THE EU INTERNAL MARKET IN THE NEXT DECADE – QUO VADIS?

Edited by **Ivan Sammut**
and **Ivan Mifsud**

BRILL

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Contents

Preface

This edited book results from an academic Jean Monnet Chair Project under the academic direction of the editor, Professor Ivan Sammut, entitled *The EU and its Citizens – Knowing your rights under EU law*. The Project is run by the Faculty of Laws of the University of Malta through the European and Comparative Law Department.

The European Internal Market is one of the EU's greatest achievements. It has fuelled economic growth and made the everyday lives of European businesses and consumers easier. It comprises the 27 Member States and sees the participation of the other states of the EEA plus other third countries that are either seeking membership of the EU or are seeking close trade agreements. The EU's economic Union, called the 'Internal Market', is not just about the four traditional freedoms of goods, persons, services, and capital but is also about the harmonisation and/or unification of various other aspects of economic policy. The EU started as a common market and is constantly evolving into a stronger economic union since the Maastricht amendments of the early 1990s. However, the evolution of the Internal Market does not stop. With the widening and deepening of competencies after the Lisbon Amendments 2009, the momentum is still ongoing more than a decade later.

The Department of European and Comparative Law within the Faculty of Laws of the University of Malta has embarked on a project to examine the current state of the Union *vis-à-vis* the EU's Internal Market and the way forward. This edited volume presents selected essays dealing with the state of affairs of the Internal Market at present and in the future (full details below). The authors are either resident academics at the Faculty or practitioners who work in the respective field of law and give their services to the mentioned Faculty. The work is directly relevant to practitioners and academics working in the field covered by the selected topics. Also, it will prove highly relevant to undergraduate and post-graduate students who want to read further and supplement their basic textbooks. Above all, the work should interest any stakeholder in the EU's Internal Market.

The book is divided into three parts. Part I focuses on citizens' rights, while Part II looks at citizens' rights from the point of view of digital rights. Part III focuses more on other substantive issues of the Internal Market. This edited book represents the work undertaken by the University of Malta during this Project. The opinions of the papers in the book reflect solely those of the respective author and not of the editors.

Ivan Sammut

Abbreviations

AFSJ	Area of Freedom, Security and Justice
AG	Advocate General
AI	Artificial Intelligence
A29WP	Article 29 Working Party
B2B	Business-to-Business
B2C	Business to Consumers
CARIN	Camden Asset Recovery Inter-Agency Network
CEN	European Committees for Standardisation
CENELEC	Electrotechnical Standardisation
CESL	Common European Sales Law
CEUE	Corpus of EU English
CFR	Common Frame of Reference
CPC	Consumer Protection Cooperation
CRD	Consumer Rights Directive
DGT	Directorate General for Translation
DMA	Digital Markets Act
DPIA	Data Protection Impact Assessment
DSA	Digital Services Act
ECHR	European Convention on Human Rights
ECtHR	European Court of Human Rights
EEA	European Economic Area
EDPB	European Data Protection Board
EDPS	European Data Protection Supervisor
EPL	European Private Law
EPPO	European Public Prosecutor Office
EU	European Union
EAW	European Arrest Warrant
EIO	European Investigation Order
FATF	Financial Action Task Force
GDPR	General Data Protection Regulation
GPAI	General Purpose Artificial Intelligence
IATE	Interactive Terminology for Europe
IMI	Internal Market Information System
IMO	Internal Market Ombudsman
LLM	Large Language Model
NLP	Natural Language Process
RAILS	Robotics And AI Law Society
OUP	Oxford University Press
PCRB	Public Contracts Review Board
SME	Small and Medium-Sized Enterprise

TEC	Treaty on European Communities
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
TRIS	Single Market Transparency Directive (EU) 2015/1535
UCITS	Undertaking for Collective Investment in Transferable Securities

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was admitted to the bar in 2004. He completed his PhD studies at the University of Groningen in 2023, having submitted a thesis on EU public procurement under the supervision of Professor Laurence Gormely. Throughout his professional career, Dr Joseph Bugeja has occupied the Director of International Economic Relations at the Economic Policy Division within the Ministry of Finance from September 2004 to June 2012. He represented Malta as a titulaire of the Trade Policy Committee (Council committee established by Article 207 of TFEU). He also occupied the Director (Land) position from July 2012 to December 2014 and Commissioner of Land from December 2013 to 2014. In addition, Dr Bugeja practices as an advocate in front of the Maltese law courts and tribunals and provides legal consultancy services. He became a full-time resident academic at the Department of European and Comparative Law, the University of Malta, in October 2020.

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Introduction

Ivan Sammut

The Internal Market, initially a common market, has existed since 1 January 1958. Following the Maastricht Treaty in 1994, the EU evolved from a Common Market into an economic union, known as the Internal Market, to signify a union without internal borders. In 2024, Pierre-Yves Dermagne, Belgian Deputy Prime Minister and Minister of the Economy and Employment, said that the Internal Market is one of the main achievements of the European Union. It has provided benefits to our social welfare and reinforced our global economic position. But we should not be complacent: the single market is still fragmented, not everyone benefits equally, and big players impose their own rules. The conclusions adopted today draw a roadmap to strengthen our single market and prepare it for the incoming global challenges.[1]

The Council's conclusions acknowledge the achievements of the single market in the 30 years of its existence but also recognise the need for a new strategy to harness its untapped potential. The Council, therefore, called on the Commission to prepare a strategy for a modernised single market before June 2025. The conclusions identify the need for a more efficient regulatory framework adapted to the green and digital transitions and fast-changing global realities. To meet that need, the Council calls for removing unnecessary administrative burdens and compliance obligations (i.e. excessive reporting). The conclusions also call for identifying and withdrawing obstacles to the growth of companies, including SMEs, and applying digital solutions in future regulation (principles like 'think small first', 'once only', 'digital by default' or the SME passport).[2]

Ministers call for better use of tools like SOLVIT centres (a support service to help companies and citizens facing problems in another Member State). The conclusions call for the prevention of over-regulation, the permanent monitoring of the market situation, and the coherent and strong enforcement of existing legislation. It also calls for addressing unfair commercial practices to strengthen consumer protection. Ministers also underlined the importance of better regulation, with timely, useful, and dynamic impact assessments,

1 https://www.consilium.europa.eu/en/press/press-releases/2024/05/24/council-adopts-conclusions-on-the-future-of-the-single-market/ last accessed on 28th May 2024.

2 https://www.consilium.europa.eu/en/press/press-releases/2024/05/24/council-adopts-conclusions-on-the-future-of-the-single-market/ last accessed on 28th May 2024.

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broad consultations (including citizens' panels) and the use of regulatory sandboxes – temporary legal frameworks which allow the testing of innovative technologies, products, services or regulatory approaches.

The conclusions also call for several measures to enhance the single market's potential, such as the better use of private and public investment, joint public and private strategic investments, and public procurement. The conclusions also propose removing barriers to cross-border services by applying simplified procedures. Ministers underline the importance of improving the capacities of the EU's workforce (with good education, training, and long-life learning) and making the single market attractive for highly skilled workers from non-EU countries. Ministers also underline the strength of the single market at the global level and emphasise the importance of making the most of its core role in the World Trade Organization and the EU's strength as a global standardisation power.[3]

2023 marked the 30th anniversary of the Treaty of Maastricht and the creation of the European single market. Since then, a comprehensive process of reflection on the opportunities and challenges it presents has been underway. The European Council of March 2023 called for ambitious action to complete the single market. In June, EU leaders requested an independent High-Level Report on the future of the single market. The Spanish and the Belgian presidencies commissioned the former Italian Prime Minister and president of the Jacques Delors Institute, Enrico Letta, to draw up the report. The final version, 'More than a Market', was presented at the Special European Council on 17 and 18 April 2024.[4]

On 24 May 2024, the Council of the European Union reached the following conclusions among others:[5]

1 The Need for a New Horizontal Strategy for the Single Market

HIGHLIGHTS the central role of the Single Market as a driving force of European integration, sustainable and inclusive growth as well as the Union's global strength; In this regard, UNDERLINES the need for a fully functioning Single Market as an essential prerequisite for long-term competitiveness and

3 https://www.consilium.europa.eu/en/press/press-releases/2024/05/24/council-adopts-conclusions-on-the-future-of-the-single-market/ last accessed on 28th May 2024.

4 https://www.consilium.europa.eu/en/press/press-releases/2024/05/24/council-adopts-conclusions-on-the-future-of-the-single-market/ last accessed on 28th May 2024.

5 https://data.consilium.europa.eu/doc/document/ST-10298-2024-INIT/en/pdf last accessed on 28th May 2024.

prosperity, to achieve the fair green and digital transitions, ensuring a level playing field that leaves no one behind; STRESSES the need to include concrete steps towards further integration, removing unjustified or disproportionate barriers – especially for services – and preventing restrictions to free movement in a new horizontal Single Market strategy; HIGHLIGHTS that a fully functioning Single Market must be based on the principle of subsidiarity and proportionality;

REITERATES that to maintain the Union's economic security, resilience and competitiveness, more work is needed to revitalise the Union's social market economy and its industrial base, further enhance the Union´s connectivity and strengthen the resilience of its supply chains, as well as to boost its technological leadership and attractiveness as a business location and a labour market, where SMEs can innovate, scale up and prosper; EMPHASISES that a strategic geopolitical vision must be given to the Single Market to guarantee the achievement of these goals, its strategic autonomy, while preserving an open economy, and attaining climate neutrality;

2 Investing in the Fair Green and Digital Transitions

While ensuring a level playing field within the Single Market and promoting it globally, UNDERLINES the need for mobilising a combination of both private and public financing, including the creation of truly integrated European capital markets, to support the fair green and digital transitions and to stimulate the growth potential of European businesses, and that the Union's budget and the EIB group continue to play an important role; STRESSES the urgency to boost the Union's global competitiveness and attractiveness;

INVITES the Commission to undertake an in-depth analysis of the existing public procurement legislative framework towards resilient and sustainable public procurement and effective competition, to assess whether a revision is necessary during the 2024–2029 term in light of the major commitments that the EU made in order to achieve its sustainable development objectives by 2030, while promoting the fair treatment of European suppliers;

3 Delivering on Cross-Border Services and Fostering High-Quality Jobs

STRESSES that significant untapped opportunities lie in the area of services and

UNDERLINES the need to remove fragmentation, and to simplify the rules for cross-border provision of services, not limited to the scope of the Services

Directive, to achieve the full opportunities of the services sector, while ensuring workers' rights, by:

focusing on horizontal and economically significant services, especially in professional and business services, in light of servitisation;

STRESSES the valuable contribution of the social economy to strengthen the Single Market in making the fair green and digital transitions more inclusive and rooting them in local communities;

CALLS ON the Commission, the Council and the Member States to follow-up on these Council Conclusions towards a constant improvement and integration of the Single Market through the annual policy cycle for the Single Market and competitiveness; INVITES the Commission to base itself on an improved Annual Single Market and Competitiveness Report which reflects practices and challenges of businesses and citizens;

CALLS ON the Commission to adopt a new horizontal Strategy for a modernised Single Market by June 2025 with the aim to reduce fragmentation and complete the Single Market across policy areas, including a roadmap with clear timelines and milestones for urgent and concrete actions across all policy areas, based on facts and needs from businesses, social partners, stakeholders and citizens, focusing on redundant, incoherent or burdensome rules;

INVITES the Commission to develop technical and factual analyses of the recommendations in the High-Level Report across all relevant policy areas and invites the Member States and the Commission to examine these in-depth and identify key recommendations; The current and future Council Presidencies will take work forward on the identified recommendations on the basis of these analyses, with a view to creating an area without internal borders in which the free movement of goods, persons, services and capital is ensured for the benefit of all;

INVITES the incoming Council Presidencies to ensure the follow-up of these Conclusions in close coordination with the relevant working groups.

This book addresses some of the issues mentioned in the Council of the European Union meeting on 24 May 2024. It selects some topics highly relevant to the Internal Market and the citizens' rights *vis-à-vis* the Internal Market and explores the way forward in the next decade. Part I deals with a selection of papers on Citizens' Rights. Part II deals with a selection of papers on digital rights and Artificial Intelligence (AI), which will be the Internal Market's challenge in the next decade. Finally, Part III deals with a selection of substantive rights within the context of the Internal Market.

PART 1

Citizens' Rights

CHAPTER 1

SOLVIT – The Entity without a Face

Ivan Mifsud

Abstract

The title of this article is a play on the first incumbent European Ombudsman's claim when taking office that his institution would serve to give the European Administration a more human face; the actual article finds its inspiration in a proposal made in the 1990s by a certain Stephen Harris, for the setting up of an Internal Market Ombudsman. While this never materialised, several entities were created to help individuals and businesses navigate the Internal Market. At the forefront of these is SOLVIT, which does not qualify as an Internal Market Ombudsman but helps resolve cross-border issues that businesses and individuals experience. On the other hand, one finds the European Ombudsman, which, although an 'ombudsman' does not, and indeed never was intended to, assume the role of an Internal Market Ombudsman. The author explores both SOLVIT's and the EU Ombudsman's histories, evolution, activities, and achievements before comparing the two institutions and queries whether there is still a need for an Internal Market Ombudsman.

1 Introduction

The starting point to this chapter was an article called *The Need for an Internal Market Ombudsman*[1] the author of which called for the creation of an ombudsman-style entity 'to provide impartial guidance on the interpretation and application of relevant directives'; this suggestion was aimed at avoiding lengthy and expensive court proceedings when issues concerning the correct, uniform interpretation and application of directives arose. The idea proposed was to create an expeditious, user-friendly, inexpensive, authoritative, highly respected, independent and impartial 'mediator, facilitator and arbiter all rolled into one'[2] which could provide cheaper and faster answers than the Court of Justice of the European Union could. Stephen Harris expressed concern that this Internal Market Ombudsman (IMO) will introduce a new layer of

1 Harris, Stephen EIPASCOPE, 1999 (1) 1–7.
2 *Ibid.*

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bureaucracy, might complicate processes, and, worst of all, might not deliver as expected; he also acknowledged the existence of the European Ombudsman but correctly observed that 'cases concerning the need for impartial guidance on directives' requirements would seem inappropriate for reference to the European Ombudsman. A new, different office is therefore needed.[3]

Stephen Harris' idea of an ombudsman institution is rather particular in the sense that while ombudsmen do indeed guide their customers, they are not in the business of giving formal advice on the lines he proposed; indeed, his proposal is more akin to some form of advisory bureau than an ombudsman.

Fast forward a quarter of a century to the present day, and one observes the number of entities created since the article in question was written, all of which serve both individuals and businesses in navigating the European Single Market, mitigating the need to resort to costly and lengthy judicial proceedings, namely: EU Pilot,[4] CPC,[5] TRIS,[6] Your Europe,[7] Your Europe Advice,[8]

3 Harris, N1.

4 'A mechanism for informal dialogue between the Commission and the Member State concerned on issues relating to potential non compliance with EU Law. It is used before a formal infirngement procedure'. (*European Commission Single Market Scoreboard* https://ec.europa.eu/internal_market/scoreboard/_docs/2021/12/governance-tools/eu_pilot_en.pdf accessed on 27th December 2023.

5 'The Consumer Protection Cooperation (CPC) Network consists of **authorities** responsible for enforcing EU consumer protection laws to protect consumers' interests in EU and EEA countries'. (*European Commission Single Market Scoreboard* https://ec.europa.eu/internal_market/scoreboard/_docs/2021/12/governance-tools/cpc_en.pdf accessed on 27th December 2023).

6 'The Single Market Transparency Directive (EU) 2015/1535 serves to prevent regulatory barriers arising in the internal market for products and information society services. EU Member States and other participating countries notify their draft rules in those fields to the Commission. This triggers a 3-month standstill period during which the Commission and other countries assess the national draft rules in light of EU rules. If they identify a potential barrier to the single market, they can respond. Any concerns they identify can then be addressed'. (*European Commission Single Market Scoreboard* https://ec.europa.eu/internal_market/scoreboard/_docs/2021/12/governance-tools/tris_en.pdf accessed on 27th December 2023).

7 'The Your Europe portal helps people and businesses in the EU by:
- providing clear **information on their rights and obligations** in the Single Market
- **giving access to assistance services** in case they need help'. (European Commission Single Market Scoreboard https://ec.europa.eu/internal_market/scoreboard/_docs/2021/12/governance-tools/youreurope_en.pdf accessed on 27th December 2023).

8 'Your Europe Advice is an EU-run advisory service answering citizens' and businesses' queries (by phone or online) about their EU rights in the Single Market. It relies on a network of about 60 legal experts who handle enquiries in all 24 official EU languages'. (*European Commission Single Market Scoreboard* https://ec.europa.eu/internal_market/scoreboard/_docs/2021/12/governance-tools/yea_en.pdf accessed on 27th December 2023).

IMI,[9] E Certis[10] and SOLVIT.[11] They are all extremely relevant, but out of them all, SOLVIT seems to be the closest not to what Harris proposed all those years ago but to this author's idea of what an Ombudsman does; Harris' article led the present author to query whether there exists a need for an IMO in the true sense of the term that is, as a complaints handler and promoter of good practices.

In this present article, the author will explore SOLVIT's history, evolution, activity and achievements and will compare them with those of the European Ombudsman; their roles are different, and the European Ombudsman is not an alternative to SOLVIT, but on the other hand, the European Ombudsman is the closest existing model to the IMO even if not as Stephen Harris proposed. The idea behind this present article is to bring out the strengths and weaknesses both of SOLVIT and of the European Ombudsman, ultimately answering the question: whether there is a need for an IMO as a complaints handler and awareness raiser, or whether SOLVIT has filled the lacuna and if so, whether it has been filled adequately.

As for the title of this article, it is intended as a play on Jacob Söderman's claim back in 1995, when taking the oath of office as the first European Ombudsman, that his institution would serve to give the European Administration a more human face.[12] The title ties up with whether SOLVIT, which, unlike any ombudsman institution, lacks a 'face', adequately fills the brief.

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9 'The Internal Market Information System (IMI) is an IT application that connects national, regional and local authorities across the EU (EEA). IMI allows authorities to communicate quickly and easily with their counterprts abroad'. (*European Commission Single Market Scoreboard* https://ec.europa.eu/internal_market/scoreboard/_docs/2020/07/performance_by_governance_tool/imi_en.pdf accessed on 27th December 2023).

10 'Do you work for an EEA-based company wishing to participate in a public procurement procedure? Or are you a public buyer evaluating bids received from various EEA countries? If so, eCertis can help …' (*European Commission Single Market Scoreboard* https://ec.europa.eu/internal_market/scoreboard/_docs/2020/07/performance_by_governance_tool/e-certis_en.pdf accessed on 27th December 2023).

11 'SOLVIT is a service offered by the **national administrations.** There is a SOLVIT centre in each EU Member State and in Iceland, Liechtenstein and Norway. They work together via an online database. SOLVIT helps people and businesses who encounter difficulties in another EU Member State when public authorities do not apply EU legislation correctly'. (*European Commission Single Market Scoreboard* https://ec.europa.eu/internal_market/scoreboard/_docs/2020/07/performance_by_governance_tool/solvit_en.pdf accessed on 27th December 2023).

12 *The European Ombudsman, Origins, Establishment, Evolution,* 1995, Luxembourg Office for the Official Publications of the European Communities, 1.

2 SOLVIT's History, Evolution, Activities and Achievements

The initial step leading to the entity we have today finds its roots in the 1997 'Action Plan for the Single Market',[13] Phase One of which included the 'creation of a framework for enforcement and problem-solving'.[14] This framework of centres in each Member State came into being; however, SOLVIT as we know it resulted after the European Commission's 2001 Recommendation 2001/893/EC,[15] which led to the setting up of an online database shared between the 'Coordination Centres' and the establishing of the principles to be followed when processing, to resolve, cross-border issues brought before them from the first step when the Centre gets news of the very existence of the problem. This recommendation aimed at standardising procedures between all Member States and ensuring transparency for users and potential users to know how these centres operate. Years later, the European Commission made a recommendation, dated 17th September 2013,[16] which was intended to further reinforce SOLVIT given the increased workload over the years.

SOLVIT commenced operations on 22nd July 2002.[17] Since then, the aggrieved individual or business merely has to complete an online application, which, apart from being straightforward, is also standard because it is the same one for all persons, reflecting the fact that SOLVIT is one entity under the European Commission with branches in each of the Member States together with Iceland, Liechtenstein and Norway; thus for example whether one tries to access SOLVIT via the European Commission website,[18] or after googling the Maltese SOLVIT Centre as the author of this article did, the system leads to the very same complaint form[19] which is available in twenty-five different

13 https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=LEGISSUM%3Al70002#:~:text=In%20view%20of%20this%2C%20the,in%20the%20new%20technological%20environment last accessed on 27th December 2023.

14 *Ibid.*

15 https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A32001H0893 accessed on 27th December 2023.

16 https://ec.europa.eu/solvit/_docs/2013/20130917_recommendation_solvit_en.pdf accessed on 27th December 2023.

17 *SOLVIT's Helping Hand in the Single Market: celebrating 20 years* p.7. Available at https://ec.europa.eu/docsroom/documents/51374 last accessed on 27th December 2023.

18 https://ec.europa.eu/solvit/index_en.htm accessed on 27th December 2023.

19 https://ec.europa.eu/eu-rights/enquiry-complaint-form/home?languageCode=en accessed on 27th December 2023.

languages. Once the form is filled in, it goes to the 'Home Centre', the SOLVIT centre in the complainant's country.[20]

These centres all form part of the national public administration of the particular country to the extent that they are even financed by the member state with other support such as training and materials provided by the European Commission; as 'home centres' they are obliged, if they require further information, to contact the complainant within one week of receipt of the complaint; they will also check that the complaint falls within SOLVIT's remit and send it to the 'Lead Centre' this being the country in which the problem occurred. The Lead Centre will confirm whether it accepts the complaint within one week, and will try to find a solution with the responsible authority. The target is to solve the problem within ten weeks after the Lead Centre accepts the complaint. Procedures are free of charge; the Home SOLVIT Centre is obliged to keep the complainant informed as the case progresses, while the complainant is free to contact the Home Centre for an update.[21] The full list of centres, including their physical address, email addresses and contact telephone numbers, is available online.[22]

The European Commission website[23] seeks to maximise transparency, including annual reports from as far back as 2004, policy documents, the 10th anniversary evaluation report, and the 20th anniversary report. These documents are prepared at the EU level and not at the national level because, as already stated, SOLVIT is one European entity with branches in different states, not an association of individual complaints handling centres. From these reports and other documents one learns a lot about SOLVIT, including how from a caseload of a mere 38 complaints received in 2002, its caseload shot up to 2,271 complaints in 2022; one learns about its average 88% resolution rate with some countries actually enjoying a 100% resolution rate; how the bulk of cases are received from individuals and not from businesses to the extent that while the number of cases lodged by individuals has increased over time those lodged by businesses have remained practically constant since SOLVIT's inception; one also reads about the staff shortages, the high numbers of tasks to perform and high staff turnover at some of the centres and the observation made

20 Thus for example, a complaint form filled by a Maltese national, or filled on behalf of a Malta-registered company, will go to the Maltese Centre.

21 https://ec.europa.eu/solvit/how-solvit-works/index_en.htm accessed on 27th December 2023.

22 https://ec.europa.eu/solvit/contact/index_en.htm accessed on 27th December 2023.

23 https://ec.europa.eu/solvit/index_en.htm accessed on 27th December 2023. SOLVIT is serviced by only one website, in the sense that the national centres are all part of one system, to the extent that they do not have their own websites.

that 'this has an impact on the quality of case handling … (and) holds SOLVIT back from developing its full potential':[24] this appears to be a reprimand from the European Commission to certain individual members of the Single Market, aimed at getting them to up their game, and it is indeed ironical that these individual countries who are supposedly so committed to the Single Market inadequately staff that very same entity set up to help forward the same Market.[25] A comparison between the 2021 annual report[26] and 2022[27] indicates an improvement, at least in certain countries such as Iceland, which seems to have resolved the issue between 2021 and 2022.

One also reads about the type of cases handled by SOLVIT and the issues they have encountered, including difficulties for nurses to get registered in Ireland due to language requirements, delays in the organisation of aptitude tests for physiotherapists in the Netherlands, discriminatory insurance requirements for Polish ski instructors in Italy, discriminatory conditions to complete professional registration as a bus driver in Cyprus, refusal of foreign bank accounts for the payment of taxes in France, delays in the exchange of foreign driving licenses in France and Portugal and difficulties in Sweden experienced by people from other EEA countries in registering in the population register and obtaining a personal identification number which is necessary to gain access to certain essential services.[28]

One cannot be positively impressed when reading about SOLVIT's work and achievements. On the other hand, one senses that the organisation is what it is in that the national centres are branches of their respective countries' civil service, which brings particular constraints, especially regarding outreach.

Online searches conducted by the author of this article into the national centres of the Republic of Ireland, Italy, Malta and France[29] revealed similar trends in the sense that all four centres carry out a certain amount of outreach work. Thus, for example, *SOLVIT Italia,* which forms part of the *Dipartimento*

24 https://single-market-scoreboard.ec.europa.eu/enforcement-tools/solvit_en accessed on 27th December 2023.

25 https://single-market-scoreboard.ec.europa.eu/enforcement-tools/solvit_en accessed on 27th December 2023.

26 https://ec.europa.eu/internal_market/scoreboard/_docs/2021/12/governance-tools/solvit_en.pdf p.3 accessed on 28th December 2023.

27 https://ec.europa.eu/internal_market/scoreboard/_docs/2022/12/enforcement-tools/solvit_en.pdf p.3 accessed on 28th December 2023.

28 *Ibid.*

29 Which countries were chosen owing to language constraints.

per gli Affari Europei,[30] has links with other entities such as Assolombarda[31] and with the *Camera di Commercio di Lucca*,[32] both of which promote its services amongst their members, on the other hand, while forming part of the Department of Trade, Enterprise and Employment, the Irish SOLVIT Centre has its stand-alone website[33] albeit old-fashioned and somewhat outdated in terms of content, the last press report harking back to 2nd October 2019, and with some of the links broken. Old and outdated as the Irish website may be, it includes reports of its Centre taking part in promotional events such as organising information stands from which information and advice were given to businesses;[34] similarly, SOLVIT Malta is part of the Commerce Department and just like its peers carries out some outreach, for example, having participated in the Europe Direct Gozo 2022[35] and Europe Day Expo 2023;[36] the French SOLVIT Centre forming part of the *Secrétariat Générale des Affaires Européennes*[37] has links which include with the *Fédération Française du Bâtiment*.[38] Such outreach, while commendable, comes across as being what one may expect from organisations which do their best with the available resources and within the confines of a larger bureaucratic machine, as opposed to the outreach and marketing of entities which enjoy independence and, being adequately resourced, boast well-oiled public relations facilities. It is indeed regrettable that this limited outreach seems to have persisted despite the 2017 European Commission Action Plan for the Reinforcement of SOLVIT,[39] which, amongst other things, included 'increasing awareness raising activities';[40] indeed, this is reflected in

30 Department for European Affairs.
31 Association for Industry in Milan, and in the provinces of Lodi, Monza & Branza, and Pavia https://www.assolombarda.it/ accessed on 28th December 2023.
32 Lucca chamber of commerce.
33 https://www.solvitireland.ie/ accessed on 28th December 2023.
34 https://www.solvitireland.ie/press-promotion/ accessed on 28th December 2023.
35 https://europedirectgozo.org/event/network-of-networks-meeting/ accessed on 28th December 2023.
36 https://sem.gov.mt/latest-updates/news/europe-day-may-9-2023 accessed on 28th December 2023.
37 General Secretariat for European Affairs.
38 French Federation for the Construction Industry https://www.ffbatiment.fr/ accessed on 28th December 2023.
39 https://ec.europa.eu/solvit/_docs/2017/com-2017-255_en.pdf accessed on 28th December 2023.
40 *Ibid*., 6.

the figures: SOLVIT caseload remained virtually unchanged year on year since 2014[41] indicating that the 2017 action plan did not lead to higher caseloads.

3 The European Ombudsman's History, Evolution, Activities and Achievements

The European Ombudsman was set up under the Maastricht Treaty of 1992, and the first incumbent was appointed in 1995.[42] This institution is regulated by Article 228 of the Treaty on the Functioning of the European Union.[43] It concerns itself with instances of maladministration in the activities of the Union institutions, bodies, offices or agencies, except for the Court in its judicial role. Complaints may be lodged by any Union citizen and any other person, whether natural or legal, residing or having a registered address in the Union. The Ombudsman examines such complaints and reacts accordingly; many complaints are out of jurisdiction, but some will merit inquiry.[44] The European Parliament appoints the European Ombudsman after the first election of the Parliament and for the duration of its term of office; incumbents, however, are eligible for reappointment. The European Ombudsman reports back to the European Parliament and enjoys a very strong security of tenure, being only dismissible by the Court of Justice of the European Union on the request of the Parliament 'if he no longer fulfils the conditions required for the performance of his duties or if he is guilty of serious misconduct'.[45] The incumbent must be completely independent in performing their duties, cannot take instructions from anyone during the term of office, and cannot engage in any other occupation, whether gainful or otherwise.[46]

41 https://ec.europa.eu/solvit/_docs/2022/anniversary_report_print_en.pdf p.12 2368 cases in 2014 (up from 1430 in 2013), 2228 cases in 2015, 2414 cases in 2016, 2079 cases in 2017, 2295 cases in 2018, 2380 cases in 2019, 2633 cases in 2020 and 2455 in 2021.

42 Since creating the European Ombudsman, three persons have held this position: Jacob Söderman from Finland (1995–2003), P. Nikiforos Diamandouros from Greece (2003–2013) and present incumbent Emily O'Reilly from the Republic of Ireland.

43 TFEU. https://www.ombudsman.europa.eu/en/legal-basis/treaties/en accessed on 29th December 2023.

44 Thus for example in 2021 out of 2192 registered complaints, 1400 fell outside the European Ombudsman's mandate, while 332 inquiries were initiated (Annual Report for 2021 available at https://www.ombudsman.europa.eu/en/doc/annual-report/en/156017 accessed on 3rd January 2024).

45 Art. 228(2).

46 Art. 228(3).

The EU Ombudsman is also subject to Regulation (EU, Euratom) 2021/1163,[47] which regulation aims at covering every aspect of their operations, including election and appointment,[48] remuneration,[49] dismissal,[50] complaints handling and own initiative inquiries,[51] the obligation to collaborate with the Ombudsman,[52] procedures following findings by the Ombudsman[53] and administrative set up including right to an adequate budget and staffing.[54] The same institution is further regulated by 'Implementing Provisions', which emanated from the European Ombudsman's office itself[55] which provisions go into the finer details of the operation; for example, whereas Regulation 2021/1163 stipulates that people may complain to the Ombudsman,[56] the implementing provisions require that the complaint is made in writing;[57] these implementing provisions also go into other matters such as delegation of complaints handling powers[58] and cooperation with national ombudsmen from Member States.[59]

The above rules make for a well-organised and resourced ombudsman, further strengthened by Articles 41 and 43 of the Charter of Fundamental Rights of the European Union,[60] which deals with the right to good administration and access to the Ombudsman.

Overall, the above legal structure is typical of what one would expect from an Ombudsman.[61] Procedures are typical in that, like in other ombudsman institutions, the European Ombudsman receives complaints. If the complaint is accepted for investigation, the European Ombudsman will exercise her powers,

47 Art. 228(4) TFEU and https://www.ombudsman.europa.eu/en/legal-basis/statute/en accessed on 29th December 2023.

48 Art. 11.

49 Art. 15.

50 Art. 13.

51 Arts. 2 & 3.

52 Art. 5.

53 Art. 4.

54 Art. 16.

55 https://www.ombudsman.europa.eu/en/legal-basis/implementing-provisions/en accessed on 29th December 2023.

56 Regulation Art. 2.

57 Art. 2.1.

58 Art. 11.

59 Art. 12.

60 https://www.europarl.europa.eu/charter/pdf/text_en.pdf accessed on 29th December 2023.

61 All one has to do is compare with the New Zealand model (followed by practically any other country in the Commonwealth) to establish this. The NZ act is available at https://www.legislation.govt.nz/act/public/1975/0009/latest/DLM430984.html accessed on 29th December 2023.

including access to documents, full discretion during investigations and power to summon witnesses; when the European Ombudsman feels that she is ready, she will draw her conclusions, write her report, make recommendations as necessary and follow up the same with those concerned with a view to getting as many of these recommendations as possible implemented. The fact that Parliament appoints the European Ombudsman, who reports to the same is also typical Ombudsman, as are the security of tenure, professional secrecy, equating of salary and employment conditions with those of a judge, avoidance of conflicts of interest, prohibition of external influences on her work, and the possibility of undertaking own initiative investigations.

In terms of activities, the European Ombudsman dedicates considerable time to investigating complaints received; it is reported that the European Ombudsman opens about 350 inquiries every year,[62] actually handling 2,238 complaints in 2022 alone;[63] concerning ombudsman inquiries, the same institution even goes so far as to document and give publicity to the impact of said work, via a detailed document published online[64] which distinguishes between how a situation was, and how it evolved post-ombudsman intervention, the underlying message being that the European Ombudsman can, and does indeed make a difference to peoples' lives provided the entities over which it has jurisdiction cooperate and collaborate with it as is after all their duty and obligation.

When it comes to European Ombudsman investigations, one finds several more prominent ones that received considerable media attention, such as the 'Intel' investigation[65] in which the Ombudsman found that the European Commission had infringed principles of good administration during an investigation into this chip producer, by failing to make an 'adequate written note'[66] on an important meeting held in August 2006 with a major buyer of Intel's products; according to Intel the matters discussed at this meeting were of direct concern to the investigation into its activities which was underway at that time, and as a consequence certain exculpatory evidence was compromised. Another example of a more prominent European Ombudsman case is that decided on 23rd November 2020 on the 'BlackRock' contract, in which the European Commission was criticised for awarding a study on how

62 https://www.ombudsman.europa.eu/en/impact accessed on 29th December 2023.

63 https://www.ombudsman.europa.eu/en/doc/annual-report/en/167855 accessed on 2nd January 2024.

64 *Ibid.*

65 Complaint 1935/2008/FOR available at https://www.ombudsman.europa.eu/en/decision/en/4164 accessed on 2nd January 2024.

66 *Ibid.*

to integrate social and environmental factors into EU banking regulations to an organisation which manages over €6.1 trillion in the very same sector[67] that the European Commission had engaged it to study and make recommendations on; Ms Emily O'Reilly observed that 'winning the contract may enable the company to gain insights and assert influence over a growing investment area of major and increasing relevance to its clients, and therefore to the company itself'.[68] Ms O'Reilly concluded that the European Commission should have been more vigilant; on its part, the Commission reflected on possible amendments to financial regulations and additional guidance to assist staff dealing with public procurement procedures.[69]

European Ombudsman's strategic investigations include one into business trips by a European Commission director general to a non-EU country, for which the receiving country paid for trips. The European Ombudsman sought to ensure that any conflicts of interest were mitigated; the Ombudsman found the application of relevant rules to be 'problematic' and recommended that the Commission reflect on whether it can do more to ensure compliance.[70]

Apart from investigations, the European Ombudsman also finds considerable time to participate in events and share her views on matters of relevance to her office.[71] Such a proactive stance is admirable because it gives the ombudsman institution the exposure required to convey its values, including the right to and principles of good administration. Indeed, much emphasis is placed on such communication, using social media, and running a website that is attractive, modern, up-to-date, and highly informative. One cannot help but note that this is not only about the message but also about the incumbent, in the sense that the Ombudsman is herself given considerable prominence, hence the photos, for example, giving out the 'Award for Good Administration'

67 Described by Reuters as 'the world's largest asset manager' https://www.reuters.com/business/eu-considers-tightening-law-after-inquiry-into-blackrock-contract-2021-04-19/ accessed on 2nd January 2024.

68 https://www.ombudsman.europa.eu/en/decision/en/135363 accessed on 2nd January 2024.

69 https://www.ombudsman.europa.eu/en/news-document/en/140683 accessed on 2nd January 2024.

70 Case SI/2/2023/KR available at https://www.ombudsman.europa.eu/en/case/en/63485 accessed on 2nd January 2024.

71 The EU Ombudsman website indicates around one public speech every month at different events such as Global Ireland Summit and University of Warsaw, all delivered by the EU Ombudsman herself https://www.ombudsman.europa.eu/en/speeches accessed on 2nd January 2024.

in mid-2023[72] and of the Ombudsman herself 'at work'[73] apart from videos such as 'European Ombudsman – here to help' and 'The European Ombudsman – ensuring a transparent and accountable EU'.[74] This is done to promote the human side of the institution, the idea of a very hardworking, fair, inviting person, a reasonable troubleshooter with whom the European Union institutions can collaborate without fear and to whom the general public can relate, have faith in, and will turn to in their hour of need.[75] While all ombudsman-like institutions include such publicity and promotional material and try to come across as inviting as possible, it probably helps that the European Ombudsman has a budget appropriation of €12,222,108[76] and is backed by a staff of around ninety persons, which includes eleven persons in the Communication Unit alone.[77]

In terms of setup and contrast with SOLVIT, the European Ombudsman is not a collection of entities in the different EU and EEA countries with a common coordinating centre but is one entity based in Strasbourg with another office in Brussels; in other words, the European Ombudsman has offices wherever the European Parliament does too, as is befitting of an officer of Parliament. The European Ombudsman and her staff must reach out to all four corners of the European Union from their Strasbourg and Brussels offices, which undoubtedly takes resources and hard work and is reflected in the above-described budget and setup. The European Ombudsman has collaborative allies in every European Union member state in the form of national and regional ombudsmen with whom she collaborates through the European Network of Ombudsmen.[78] They help in investigations if and when required, such as when she investigated the Frontex 'complaints mechanism'.[79] The national and regional ombudsmen even promote her office and refer

72 https://www.ombudsman.europa.eu/en/multimedia/photos?date=2023&id=1493 accessed on 2nd January 2024.

73 *Ibid.*

74 https://www.ombudsman.europa.eu/en/multimedia/videos accessed on 2nd January 2024.

75 This formula seems to yield the desired results because, according to the 2022 annual report (N.63) apart from complaints received, the EU Ombudsman's office replied to 1,038 requests for information about their office and and advised 13,313 persons through the website's Interactive Guide in 2022 alone.

76 N.63 Annual Report for 2022 36.

77 https://www.ombudsman.europa.eu/en/office/staff accessed on 2nd January 2024.

78 https://www.ombudsman.europa.eu/en/european-network-of-ombudsmen/about/en accessed on 2nd January 2024.

79 *Ibid.*

complaints to her if these fall within her jurisdiction as opposed to theirs;[80] we are here dealing with a relationship of collaboration, not one of control: the national and regional ombudsmen are in no way subjected to the control and power of the European Ombudsman, and she is not superior to them in any way, unlike the national SOLVIT centres which although forming part of the respective national public administration, have to follow the same standards and practices in every country as directed by the European Commission.

As a result, the European Ombudsman enjoys the benefits of having collaborators at the domestic and regional level while in no way assuming any form of responsibility for or supervisory duties over her national counterparts. She enjoys the benefits without the burdens, is comfortable knowing that ombudsmen at national and regional levels follow the same standards, and works towards reaching her goals, combating injustice and upholding the right to good administration within their geographical territory. They follow the same principles and norms because they are typical to all. They help each other and work together happily, without any need for anything to be imposed on them by any supranational entity. As a result, the European Ombudsman benefits from geographical proximity when and as required, just like SOLVIT, the difference being that this comes more naturally because it is a voluntary collaboration between equals.

4 Comparisons between SOLVIT and the European Ombudsman

Both entities are complaint-handling mechanisms with a common goal, upholding a particular aspect of the Rule of Law at the European Union level, thus contributing towards creating a better, more workable, more legitimate Union. They are both concerned with the individual, with the aggrieved person or with the aggrieved business, to the extent that one could nearly say that they enjoy the same client base because it is practically the very same people and the very same businesses who can avail themselves of either SOLVIT or the European Ombudsman depending on their exigencies: when these people need to contest a national practice or decision which affects them and concerns their right to the free movement of persons, services, capital or goods, these people or businesses resort to SOLVIT; if on the other hand, they feel the need to contest a decision or action of a European institution, they may resort to the European Ombudsman. SOLVIT and the European Ombudsman

80 The European Ombudsman will reciprocate if she receives a complaint which falls within the remit of a national or regional ombudsman.

understand this and do not regard each other as competitors; indeed, they collaborate to the extent that if either receives a complaint better suited for the other, they will pass it on to the other entity. Likewise, national ombudsmen promote SOLVIT and refer matters to them if needed.[81]

Other similarities which they enjoy include that they both reach out to their potential customers, they both seek to market their services and raise awareness about the principles they stand for and seek to convey, they both also offer their services free of charge; they are also alternative remedies to the courts even if as such are somewhat restricted in their output in the sense that ultimately they lack executive authority and rely on collaboration from the very same subjects which they investigate in order to get their conclusions and any recommended solutions actuated.

On the other hand, the officials who work within the national SOLVIT centres are not tied down by the same requirements as the Ombudsman. Although they have to be impartial and fair in their work if they are to do their job properly, there is no emphasis within SOLVIT specifically prohibiting conflicts of interest prohibiting the personnel from engaging in any other occupation while in office. Furthermore, unlike the European Ombudsman, there is no specific prohibition of external interference or undue influence over their work, as in the European Ombudsman's case, or the guaranteed budget and staffing. Within SOLVIT, there is less emphasis on these aspects because the national centres are no more than offices within the respective national public administrations required to receive complaints and try to solve them; unlike in the case of ombudsmen, there is no emphasis on the actual persons, on what they do and how they do it; if there is any emphasis at all apart from getting the complaint investigated and resolved, it is on SOLVIT itself and certainly not on any person; thus for example when a few years ago the author of this article was involved in a complaint lodged with SOLVIT, the official signed his email as "[name and surname] Malta SOLVIT Centre"; interestingly in further email correspondence the same official did not even use his SOLVIT email account, but used that of the Commerce Department where he worked, signing off as '[name and surname], Senior Principal, Commerce Department'.

The emphasis is different within SOLVIT because the scope is different. Apart from resolving issues concerning the Single Market, SOLVIT national centres being answerable to and monitored by the European Commission also serves as a means for the European Commission to learn about the shortcomings at the member state and EEA level; in other words, while solving complaints about the member states and EEA countries they are themselves under scrutiny via

81 European Ombudsman 2018 Annual Report p. 24 https://www.ombudsman.europa.eu/en/doc/annual-report/en/113728 accessed on 2nd January 2024.

the same SOLVIT, from the European Commission which is in turn subjected to the European Ombudsman's scrutiny where its activities are concerned.

5 Querying the Need for an IMO

All the similarities with the European Ombudsman do not serve to make an ombudsman out of SOLVIT. Unlike the European Ombudsman, SOLVIT is an 'internal' remedy. It is 'internal' in the sense that the executive arm of the European Union, this being the European Commission,[82] with the cooperation and collaboration of the executive governments at the national level, whether within the European Union or the European Economic Area, created a mechanism in the form of centres run by each national government within the European Union and the wider EEA, which national centres follow the same practices and collaborate to reach a common goal this being the investigation of complaints lodged by people and businesses concerning grievances related to the four freedoms and the European Single Market. Creating an ombudsman for the Single Market, in order to preserve this Ombudsman's independence and impartiality, these being inherent characteristics of any ombudsman, would require an entirely new mechanism being set up, which mechanism must be external to, and independent of, the European Commission, the national governments of the EU Member States and the EEA. A new set of rules would have to be drafted on the same lines as those establishing the European Ombudsman; this, in all likelihood, would require introducing a new provision into the TFEU, in the process not only having to justify this initiative but also resolving several matters including:

– Is there a need for an ombudsman dedicated to the Single Market? Where does this need arise from? What is wrong with SOLVIT, and what would become of it?
– Presuming the need for such an ombudsman, to whom would this new Ombudsman for the Single Market answer? Is this new Ombudsman going to answer the European Parliament, just like the European Ombudsman, and if so, on what basis? Is this done simply because all ombudsmen answer to Parliament as the democratic representatives of the People of Europe, and is this a good enough justification? Would the European Commission be ready and willing to give up this central, coordinating role over the current complaints-handling mechanism called 'SOLVIT'?
– What kind of structure would such an ombudsman-style entity require? Would one institution at a supranational level seated in a particular member

82 Together with the European Council.

state, just like all other European entities, suffice, or would there still be a requirement of local branches in each Member State and each country hailing from the EEA with a smaller supranational entity coordinating from the centre of this system?

– How much would creating such an ombudsman cost, and would the benefits justify the outlay? Would this ombudsman provide improved results regarding single market compliance and furtherance to justify the costs incurred and efforts expended?

In order to reply to the above, one needs to consider the subject matter again, this being the consolidation and strengthening of the European Single Market so aptly described by Kerstin Jorna as the European Union's 'engine room'.[83] In a different sense, the European Commission is also the European Union's 'engine room' because it is the Union's equivalent to a 'civil service' which implements the decisions taken and the direction given by the Commissioners who are comparable to Ministers and a Cabinet at national level; as this 'engine', the European Commission plays a very big part in maintaining and developing further the European Union including the European Single Market. In other words, the European Single Market, its execution, further development and overall success are largely the remit of the European Commission. With this in mind, one understands why the European Commission not only set up SOLVIT but did so in such a way that serves the dual purpose described earlier, i.e., handling complaints while directly feeding the European Commission itself with information and data about shortcomings at the national level. Creating an ombudsman-style entity would lead to the loss of this second function which SOLVIT serves, and losing this would not benefit the European Commission at all.

Suppose one had to cast aside the utility of SOLVIT to the European Commission for a moment and consider the matter purely from a complaints-handling perspective. In that case, there might be scope for arguing that the creation of an IMO, providing it with sufficient resources and appointing the right person to head it should lead to more awareness-raising on the Single Market, on the obligations of the countries which form part of this Single Market, and on the general public and businesses' rights within the said Single Market. Given sufficient resources, ombudsmen can be trusted to get this part of their job right because it is inherent to what every ombudsman does. This awareness raising would yield results, most probably in the form of more complaints being received than SOLVIT did, and hopefully also in the form of more compliance with single market rules and requirements on the national authorities.

83 Director-General of DG-GROW in her *Foreword* to SOLVIT's 2022 annual report https://ec.europa.eu/solvit/_docs/2022/anniversary_report_print_en.pdf accessed on 26th December 2023.

This is probably the biggest strength which an ombudsman would have to offer over the current SOLVIT arrangement, and linked with it is the 'face' of the institution: given the proliferation of ombudsman institutions on a global basis, the formula, which includes not only particular emphasis on awareness raising but also that element of personalisation by giving prominence to the incumbent, is proven to be effective. This, of course, would come at a huge financial cost if it is to prove effective, a cost incomparable with that of the European Ombudsman: like the European Ombudsman, this IMO would have to reach out to and raise awareness amongst the general public in all of the European Union; on the other hand, while the European Ombudsman scrutinises the European institutions, an IMO would have to scrutinise the actions and decisions of governments within every single country which is part of the European Single Market this being a much larger task if the IMO is to keep an ear on the ground, keep up-to-date with the actions of those falling under his scrutiny and if expected to raise a warning flag himself and on his initiative like any other ombudsman does, not merely waiting for complaints to arrive and then process them. Such an IMO would need at least one branch in each country, possibly more in larger countries, which must be financed by the European Union itself and not by the national governments if they are to retain independence and impartiality as every other Ombudsman does, running a central organisation with a minimum of thirty branches at the national level will not come cheap; it would also prove very complex for the IMO, the actual incumbent, to coordinate such a large organisation and to operate effectively.

An alternative, just as expensive but possibly less complex to run, would be to set up an independent IMO in each member of the European Union and EEA country; if this IMO emulates the SOLVIT model, they would benefit from a certain amount of standardisation, for example of complaints forms and procedures. Either way, an IMO would be very expensive and complex, to the point that, given the measure of success of SOLVIT, it would make more sense to invest more in the current setup to resolve and overcome its current limitations and help it develop more 'ombudsman-like' characteristics such as placing more emphasis on awareness raising, on guidance whether of individuals or businesses, on prevention and possibly also on conducting own initiative inquiries.

6 Closing Observations

Creating a proper ombudsman to deal with complaints concerning the European Single Market might make sense in an ideal world where money is no object. However, it is doubted that such an institution could ever assume the

role proposed by Stephen Harris,[84] providing guidance and interpretation of legislation related to the Single Market: it is one thing to resolve grievances, thus avoiding the need to go to Court, and another to try to create an institution which provides such authoritative interpretations of legislation that those affected will bow down and comply. The latter is unrealistic because whoever disagrees with the interpretation is bound to challenge it in Court, thus beating the whole purpose of having such a mechanism. At the same time, the former would prove too expensive and complex to justify substituting SOLVIT.

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84 N.1.

CHAPTER 2

The European Ombudsman and the Internal Market: Where Is the Connection?

Ivan Mifsud

Abstract

In this chapter, the author argues that with the European Commission – overseer of the Internal Market – accused, amongst other things, of being caught 'asleep at the wheel', the need arose for the creation of yet another institution to watch over the European Commission, to continuously prompt the European Commission and putting right any shortcomings leading to the same European Commission's performance improving, to the benefit of the Internal Market and European integration in general, and of the European Citizen. This role was awarded to the European Ombudsman, who has devised methods for going about this, including rather subtle ones.

1 Introduction

European integration is and has always been fragile because Europe as a continent has historically been a theatre of war and conflict in general, the cumulative result of which is an ingrained fragmentation. Robert Schuman's famous words back in 1950, "Europe will not be made all at once, or according to a single plan,"[1] and his reference to *de facto* solidarity could not have been more apt. Against such a background, establishing, developing and maintaining an internal market - the cornerstone of European Integration - would never be easy.

As Oana-Mihaela Salomia explains,[2] the European Internal Market involves the interaction of three players: the Member States of the European Union, the European Citizens and the European Commission. While the European Citizen is the ultimate beneficiary of the Internal Market and European integration,

1 Schuman Declaration May 1950 https://european-union.europa.eu/principles-countries-history/history-eu/1945-59/schuman-declaration-may-1950_en#:~:text=Key%20quotes,create%20a%20de%20facto%20solidarity.%22 accessed on 23rd March 2024.

2 *How do the European Commission, Member States and Citizens Interact in Enforcing Internal Market Rules?* Lex ET Scientia International Journal XXIX, VOL. 2/2022.

 | DOI:10.1163/9789004712119_004

the Member States, these being nations who voluntarily applied to join the European Union and were not allowed to join until they satisfied entry requirements, are now involved via the Council and European Parliament in the passing of European legislation and, once this is passed, are then required to implement European legislation, under the watchful eye of the European Commission which is entrusted with monitoring the implementation of European Union Law, and is also empowered with taking infringement proceedings against those who fail in their obligation to comply.

All Member States keep their national interests and domestic political needs well in mind while contributing to the creation of new European legislation; indeed, they have little choice because the leaders of the Member States have elections to win back home. This stark reality makes European integration harder to achieve; the same national interests and domestic political requirements are also why Member States occasionally fall back on their duty to comply with their European obligations. This is a day-to-day reality that may even worsen in times of crisis or when the Member States feel that the European Union is failing them.[3]

Kampmark and Kurečić[4] place much of the blame for how vaccine distribution was rolled out during the Covid-19 pandemic on the European Union and implicitly on the European Commission; they are not alone in this, with the European Commission being blamed for the 2021 humanitarian crisis on the Poland – Belarus Boarder,[5] and being accused of being 'asleep at the wheel' when it comes to overseeing the application of certain environmental legislation,[6] to name but a few instances. The causes of this are various and include a lack of resources at the European Commission; it is also suggested that priorities may lie elsewhere.[7]

This gives rise to a need for yet *another* entity to scrutinise the European Commission to hold it accountable for its actions and inactions and to keep it

3 *Vide* for example Binoy Kampmark and Petar Kurečić *Vaccine Nationalism: Competition, EU Parochialism, and Covid-19*, Journal of Global Faultlines, 2022 Vol. 9, No. 1, 9–20.

4 *Ibid.*

5 Maciej Grześkowiak, *The "Guardian of the Treaties" is No More? The European Commission and the 2021 Humanitarian Crisis on Poland – Belarus Border,* Refugee Survey Quarterly, 2023, 42, 81–102.

6 Samantha Ibbott, *Guardians of the Treaties or Neglectful Custodians: Flaws in EU Environmental Governance*, November 16th 2023, https://meta.eeb.org/2023/11/16/guardians-of-the-treaties-or-neglectful-custodians-flaw-in-eu-environmental-governance/#:~:text=As%20the%20%E2%80%9CGuardian%20of%20the,all%2027%20countries%20in%20detail accessed on 9th March 2024.

7 *Ibid.*

as much as possible on its toes and fulfilling its duties. This is where the European Ombudsman enters the picture. In this chapter, the author intends to discuss the function of the European Ombudsman as a continuous prompter of the European Commission and the significance of the European Code of Good Administrative Behaviour[8] as the standard to be followed by the European Commission continuously, the ultimate argument being that continuous prompting of the European Commission and putting right any shortcomings will lead to the same European Commission's performance improving, to the benefit of the Internal Market and European integration in general, and of the European Citizen.[9]

2 The European Ombudsman

2.1 *General Introduction*

The starting point in such a discussion has to be the Right to Good Administration[10] and the European Citizen's right to complain to the European Ombudsman,[11] neither of which preceded the actual setting up of the European Ombudsman as an institution; on the contrary, it was the first incumbent who successfully proposed the inclusion of these rights when the Charter of Rights of the European Union was being drafted.[12] This occurred in the 1990s; since the Lisbon Treaty in 2009, the Charter of Rights of the European Union has achieved binding status, clearly strengthening the European Ombudsman's position as a promoter of principles which have leapt from 'soft law' to harder, binding law.

Soon after convincing the authors of the Charter to include the Right to Good Administration and the right to complain to the Ombudsman, Mr Söderman went on to successfully lobby the drafting of a Code of Good Administrative Behaviour,[13] which code was first endorsed by the European Parliament

8 https://www.ombudsman.europa.eu/pdf/en/3510 accessed on 13th March 2024.

9 By way of explanation, it is to be pointed out that while under article 228(1) TFEU the European Ombudsman has the power to scrutinise "the activities of the Union institutions, bodies, offices or agencies, with the exception of the Court of Justice of the European Union acting in its judicial role", for the purposes of this chapter reference will only be made to the European Commission.

10 Article 41 of the Charter of Rights of the European Union.

11 Article 43 of the Charter of Rights of the European Union.

12 *The European Ombudsman Origins, Establishment, Evolution* Office for Official Publications of the European Communities (Luxembourg 2005) chapter 5.

13 N.8.

in 2001, and which has formed the basis of his and ensuing incumbents' work. Over time, it was updated and further refined.

Regarding operations, the European Ombudsman receives complaints or takes up issues on her[14] own initiative. Considerable effort is put into making the Ombudsman remedy as informal and accessible as possible; the complaints form, available in twenty-four languages, is easy to find on the Ombudsman's website[15] and straightforward to fill in. Once filled in, it merely has to be posted to the address provided in the same form without any payment being required.

The institutions are obliged to cooperate with the European Ombudsman when she considers there to be sufficient grounds in a complaint to merit investigating it;[16] the outcome of such investigations is a report on her findings, which report will point out any shortcomings noted and, where appropriate, recommend the taking of remedial steps. During this process, the European Ombudsman will invoke the Citizen's right to good administration and base her considerations on the European Code of Good Administrative Behaviour.

Some examples of notable European Ombudsman investigations involving the European Commission are the following:

– A complaint was lodged by the director of a German beer importing company against the European Commission over failure to give him information about a meeting held with UK officials over a matter he raised after considering an English law on 'guest beers' discriminatory against imported beers.[17] This individual had complained to the European Commission, which subsequently held a meeting with the UK authorities and a trade association. This individual asked to attend this meeting but was refused; further to this meeting, an amendment to the legislation on 'guest beers' was proposed, and the Commission closed its inquiries. This individual sought information, including the identities of the people who attended this meeting, but the Commission refused to grant such information based on data protection considerations. The European Ombudsman refused to accept this and recommended that this individual be given the information he sought;

14 Current European Ombudsman is Ms Emily O'Reilly https://www.ombudsman.europa.eu/en/emily-oreilly accessed on 13th March 2024.

15 https://www.ombudsman.europa.eu/en/make-a-complaint#SrYcZRwwAPeq accessed on 13th March 2024.

16 Regulation (EU, Euratom) 2021/1163 of the European Parliament of 24th June 2021, articles 5 on provision of information to the Ombudsman & 7 on hearing of officials and other servants.

17 Case reference 713/98/(IJH) reported at https://www.ombudsman.europa.eu/en/special-report/en/380 accessed on 13th May 2024.

– A complaint in which it was alleged that the European Commission failed to take minutes during a meeting which was part of an anti-trust investigation.[18] The European Ombudsman considered this to amount to maladministration;
– An investigation into an allegation that the European Commission failed to decide whether to initiate proceedings against Spain over illegal state aid granted to several football and basketball clubs. It was alleged that the European Commission failed to act on this complaint because one of its Commissioners was an ardent supporter of one of the clubs involved.[19] Following investigations, the European Ombudsman concluded that the European Commission had indeed failed to take a timely decision on whether infringement procedures should be initiated and that it also failed to allay fears that a Commissioner had a conflict of interest, which led to the Commission's inaction;
– A complaint on the European Commission's compliance with the Tobacco Control Convention.[20] On this occasion, the European Ombudsman upheld a complaint that the European Commission, except for the Directorate General for Health, failed under the WHO Tobacco Control Convention to be proactively transparent in its dealings with the tobacco industry and related lobbying groups. While the Juncker Commission responded by defending the current situation as legally adequate to prevent undue influence from the tobacco industry, the European Ombudsman concluded by finding maladministration on the European Commission's part, arising from its refusal to apply the proactive transparency policy of DG Health across the whole Commission. The matter was revisited some years later, leading the European Ombudsman to reach similar conclusions;[21]
– An investigation into the tender award to the "world's largest asset manager"[22] to carry out a study on integrating environmental, social and governance objectives into European Banking Laws[23] led the European Ombudsman

18 Case reference 1935/2008/FOR reported at https://www.ombudsman.europa.eu/en/decision/en/4164 accessed on 13th March 2024. This is often referred to as the *Intel* case.
19 Case reference 2521/2011/JF reported at https://www.ombudsman.europa.eu/en/doc/correspondence/en/52874 accessed on 13th March 2024.
20 Case reference 852/2014/LP reported at https://www.ombudsman.europa.eu/en/decision/en/73774 accessed on 13th March 2024.
21 Case reference OI/6/2021/KR reported at https://www.ombudsman.europa.eu/en/news-document/en/179462 accessed on 13th March 2024.
22 Case reference 853/2020/KR reported at https://www.ombudsman.europa.eu/en/case/en/57060 accessed on 13th March 2024.
23 *Ibid.*

to express serious reservations since this commercial entity had a direct financial interest in the sector. However, the European Ombudsman, having assessed current rules on public procurement, did not find maladministration on the European Commission's part and recommended that, in view of this incident, updating such rules should be considered. On its part, the European Commission replied by committing to reflect on this recommendation;

– An investigation into persons leaving employment or positions within the European institutions, including the European Commission, and taking up key positions and posts in industry. These included a former European Commission President taking up a post at Goldman Sachs Bank, a former European Banking Authority joining a banking lobby and a former Chief Executive of the European Defence Authority joining Airbus.[24] The European Ombudsman received and investigated complaints over these three instances, considering the applicable rules, which include the power to refuse to grant permission to such officials to take up such employment and how these rules were applied, making recommendations for improvement where necessary.

These above examples are to be taken in context. They occurred over the years and should not be taken as implying that everything the European Commission has ever done is wrong. On the other hand, one wonders what would have happened had there not been a European Ombudsman before whom such instances were brought to light.

2.2 *The Importance of Keeping the European Commission on Its Toes*

The above examples share a common thread, this being that they can all have a detrimental effect, whether large or small, on the Internal Market: for example, in the Internal Market, unlawful state aid is prohibited, as is undue lobbying with lawmakers; opaque decision making is also an enemy of a well-set up and functioning, evolving internal Market. These examples also confirm that the need to submit the European Commission to a watchdog is real. Like any other entity, the European Commission cannot be left to its own devices on a presumption that it will never err. Hence, there is a need for the European Ombudsman to keep the Commission on its toes. Mistakes will happen, shortcomings will occur, and it is the European Ombudsman's obligation firstly to maximise her efforts into continuously prompting the European Commission not to commit shortcomings, and secondly, when notwithstanding such

24 Strategic Initiative reference SI/2/2017/NF reported at https://www.ombudsman.europa.eu/webpub/2022/revolving-doors/en/ accessed on 13th March 2024.

continuous prompting, such mistakes do indeed happen, to offer a remedy aimed at putting right the wrongs committed.

While complaint handling and provision of remedies to aggrieved persons are important, the European Ombudsman's duty to continuously prompt the European Commission is vital. Having a strong, effective, influential ombudsman with whom the European Commission never feels comfortable is of utmost importance. It is such sentiment of discomfort that will entice the European Commission to be particularly careful in its work, to do things properly, to heed the Ombudsman's directions, and to keep in mind when making decisions what the repercussions will be if found committing maladministration. The day that such a sentiment is lost, the European Ombudsman will have lost its ability to prompt the European Commission into doing its utmost to as much as possible never commit acts of maladministration.

The main manner in which the European Ombudsman keeps the European Commission on its toes is through its investigatory function. The system allows the lodging of complaints by the general public with the European Ombudsman to be made as easy as possible. Receiving such complaints is a source of information for the Ombudsman because it is in this manner that she knows what the Commission has been up to. Undoubtedly, the European Commission is aware of this but can do nothing about it: the Ombudsman exists, and the facility of reporting matters to her. The only way to avoid such complaints and subsequent inquiries is by avoiding acts of maladministration in the first place.

Another way the European Ombudsman continues to prompt the European Commission is by continuously disseminating information about its work and the principles it upholds. The annual report of the European Ombudsman is an example of this: like any other ombudsman's annual report, the institution does not simply report on its activities, how many cases it has handled, how much budget it was allocated and how this was spent, but has turned this report into a vehicle intended to carry its message to the European Parliament to whom she reports, to the European Commission and all other entities that fall under her jurisdiction thus reminding them about their obligations, and to the general public to inform them of their rights and also to shame somewhat those who commit maladministration by naming them and recording their shortcoming. Another example of such effective, continuous dissemination of information is that disseminated via the European Ombudsman's particularly attractive, user-friendly and up-to-date website https://www.ombudsman.europa.eu/, which not only serves as a prime source of information about the office, its history and evolution, how it functions, its philosophy and teachings, its achievements and the numerous instances of maladministration which it

has identified over the years but also serves to mirror the state of the office itself, portraying it as a hardworking, efficient institution headed by a friendly looking and welcoming person who at the same time makes it crystal clear that she tolerates no nonsense.

Apart from the dissemination of information, there is also the creation of information and the taking of initiatives, which also keep the European Commission on its toes.[25] These include the annual 'Putting it Right Report', which, as the name implies, is an account of how the various institutions responded to the European Ombudsman's proposals. This initiative on the European Ombudsman's part serves to praise those who cooperate with her and likewise to shame those who do not; thus, for example, the European Commission is exposed for only accepting two out of five solutions proposed by the European Ombudsman under article 3(5) of the Statute[26] in 2019. This, not being a statistic to be proud of, should prompt the European Commission to do better in future, whether by accepting to implement such proposed solutions or by preventing a repeat of the maladministration which led to the European Ombudsman intervening in the first place. One also finds the 'Impact of the European Ombudsman' first published in 2020 and again in 2021, these being documents unashamedly intended to boost the Ombudsman's standing in the public eye, the underlying rationale being that the more influential the European Ombudsman proves to be, the more able to keep the European Commission and others she has jurisdiction over, on their toes.

If these publications were not enough, the European Ombudsman, since 2017, even organises an 'Award for Good Administration' which "recognises actions by the EU public service that have a visible and positive impact on the lives of citizens, and aims to encourage the sharing of good ideas and practices". By 2021, this award had morphed into one overall prize, four prizes in different categories with nominations assessed by an independent advisory board, and yet another prize for which the general public voted. This is a highly publicised ceremony, with the keynote speech in 2021 delivered by the President of the European Commission, Ursula von der Leyen herself.

Commendable as these publications and initiatives may be, the most important publication is the earlier mentioned European Code of Good Administrative Behaviour,[27] discussed in the next section of this chapter.

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25 And likewise all other entities which fall under the European Ombudsman's remit.

26 Decision 94/262 since then repealed and replaced by Regulation 2021/1163 "As far as possible, the Ombudsman shall seek a solution with the institution or body concerned to eliminate the instance of maladministration and satisfy the complaint".

27 N.8.

2.3 *The European Code of Good Administrative Behaviour*

This Code, intended to lay down the rules of acceptable behaviour of the officers who work within the European Union, is not only approved by the European Parliament[28] and published in thirty languages but is also written in such a way that is aimed at achieving the maximum effect in the sense of maximum adherence by those to whom it applies. One notes, for instance, the thrust in the following statement:

> As European Ombudsman, I have witnessed the integrity, dedication and humanity of many European public servants. This Code is designed to support those efforts by sharing best practice …

This continues regarding the increased awareness "of the practical business case for a citizen-centred approach" and regarding European decision-making being subjected to "unprecedented scrutiny" while expressing confidence "that the decision-making processes are in general robust enough to meet these scrutiny demands". The European Ombudsman is clearly warning the entities over which her office has jurisdiction that she is demanding a citizen-centred approach, that she expects to find evidence of integrity, dedication and humanity during her investigatory work, that she is going to up her scrutiny over these entities, and that they would do well to be up to such rigorous scrutiny. The European Ombudsman presents her position and her expectations with remarkable tact, even going so far as to thank the intended audience for considering the contents of this document and signing off "*Le gach dea-ghuí*"[29] but the immediately preceding reference to the European Citizen's fundamental right to good administration, directly enforceable since 2009, as the backbone of this Code, is the giveaway: through the niceties and tact the European Ombudsman reminds the institutions and their officials that the contents of this Code are non-negotiable and mandatory. They are also publicly available, thus serving a second purpose: the European Citizen has easy access to them and knows what to expect and what to require from the European institutions and their personnel.

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28 Decision of the European Parliament on the Regulations and General Conditions governing the performance of the Ombudsman's duties. OJ 1994 L 113, p. 15, as last amended by Decision of the European Parliament 2008/587/EC, Euratom of 18 June 2008, OJ 2008 L 189, 25.

29 Irish for "With best wishes".

The Foreword is followed by a throwback to 2012 when the European Ombudsman had condensed the expected standards of behaviour into 'five public service principles' namely:

– Commitment to the European Union and its citizens,
– Integrity,
– Objectivity,
– Respect for others, and
– Transparency.

The author of this chapter considers the above-listed principles to be nothing short of self-evident, except that when one refers back to the earlier cited examples of shortcomings and bad administrative behaviour identified by the European Ombudsman, one realises that what should be self-evident is not so much to everybody all of the time: for example, it should be obvious that minutes of meetings should be taken, and that Commissioners should not exercise their influence to do favours for football clubs, but it is not, or these cases would not have occurred.

As for the actual contents of the Code, many articles are well-established legal principles. These include respecting the principle of proportionality,[30] upholding the principles of natural justice,[31] guaranteeing due process[32] within a reasonable time,[33] equality of arms[34] and also respecting fundamental human rights;[35] in the same Code, one then finds principles of behaviour such as being courteous and trying to be helpful[36], replying to the general public in the same language,[37] and acknowledging receipt of letters or complaints within two weeks of receipt[38] that are very hard for any public entity to argue against respecting and abiding by, which gives them a force in themselves even though they not based on established legal principles. One also notes the obligation imposed on those entities to whom this Code of Good Administrative Behaviour applies to publicise the Code and its contents[39] and also the obligation to report back on the implementation of said Code within the stipulated period,[40] thus guaranteeing that those subject to it cannot leave

30 Article 6.
31 Article 8 'Impartiality and Independence' and article 19 'Duty to state the ground of decisions'.
32 Article 16 'Right to be heard and to make statements'.
33 Article 17 'Reasonable time-limit for taking decisions'.
34 Article 9 'Objectivity' and article 11 'Fairness'.
35 Article 5 'Absence of Discrimination'.
36 Article 12 'Courtesy'.
37 Article 13 'Reply to letters in the same language as the citizen'.
38 Article 14 'Acknowledgement of receipt and indication of the competent official'.
39 Article 25.
40 Article 27.

it to metaphorically speaking gather dust on the shelf hoping that it will be lost in the passages of time, but are held to account and in the process kept on their toes in true ombudsman style.

The fact that contents of the Code include the obligation to inform the general public of the remedies available to them, such as the existence of any possibility to appeal[41] and also to inform the general public of their right to complain to the European Ombudsman[42] is, in this author's opinion, pure genius in terms of keeping the institutions, bodies and agencies including the European Commission on their toes: they are not only kept on their toes by the European Ombudsman. They must furthermore feed this process by publicising their guardian and scrutinisers.

2.4 *The European Ombudsman's Complementary Role to the Courts*

The European Ombudsman and the Courts' roles have often been compared and found to overlap. While Paul Craig describes the European Ombudsman as an "extra-judicial machinery through which grievances concerning poorly performed Union administrative services can be inexpensively voiced and processed",[43] Marta Hirsch-Ziembinska[44] views the ombudsman remedy as an alternative way how to resolve disputes with the EU Administration, the main difference being that the Ombudsman does not issue binding decisions, but offers the advantages that no costs are involved and that proceedings are much less formal. To this, Spoerer and O'Ferrall[45] add that while the Courts "assesses compliance with the applicable law exclusively",[46] the Ombudsman takes a wider viewpoint in the form of assessing compliance with the principles of good administration and going beyond illegality into issues which, although legal are still not right, or not fair.[47] Proceedings before the Ombudsman are expeditious and informal compared to court proceedings; they are also investigatory and non-litigious, thus allowing the Ombudsman to take a wider view of the problem before her.

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41 Article 19.

42 Article 26.

43 *EU Administrative Law* (Oxford University Press 2nd Ed., 2014) 757.

44 The European Ombudsman's activity with regard to public access to environmental information in the context of the Aarhus Convention https://unece.org/fileadmin/DAM/env/pp/a_to_i/7th_meeting/Statements_and_Presentations/7TFAI_V_2_Developments_EO_Hirsch-Ziembinska.pdf accessed on 20th March 2024.

45 The European Ombudsman's role in access to documents https://link.springer.com/article/10.1007/s12027-022-00717-6 accessed on 20th March 2024.

46 *Ibid.*

47 Speech by Emily O'Reilly at EUI's academic seminar on the Evolving Role of the European Ombudsman https://www.ombudsman.europa.eu/en/event-document/en/165564 last accessed on 20th March 2024.

Apart from taking a wider view of issues brought before her than a court and the facility of taking up matters on her own initiative, which is something the courts cannot do, the European Ombudsman even turns to her counterparts at the national level with whom the institute she heads has formed a formal alliance called the European Network of Ombudsmen,[48] for collaboration, where European law and policy matters are concerned, conducting parallel investigations, holding regular meetings and conferences and even maintaining a system whereby if a member has a query concerning European Union Law, the European Ombudsman will liase with experts in particular from the European Commission to get these queries replied to. In this manner, the European Ombudsman has built the current system whereby the institutions over which she has jurisdiction are kept on their toes.

Here lies the main difference between the Ombudsman and the Courts: while the institutions are subjected to one court proceeding at a time every time a case is opened against them, the European Ombudsman has developed the facility of not only investigating the European Commission and the other entities over which she has jurisdiction but continuously getting back to the entities on their shortcomings, via the various initiatives taken which include awarding an annual prize for good administration, calling the institutions to report on what initiatives are taken to uphold the principles of good administration, reporting on the impact of the Ombudsman's work, raising legal matters over which the members of the network have queries, etc. These methods are made even more effective by the continuous effort to publicise her work and the moral pressure put on the European Commission and other entities falling under the European Ombudsman's jurisdiction, for example, describing the ombudsman 'critical remarks' as an indication of "triple failure".[49] Given that no public institution is keen on bad publicity, nor wants to be part of a failure, let alone a triple one, it is undoubted that these subtleties serve their purpose of keeping the institutions on their toes and in this sense, the European Ombudsman proves to be effective at guarding the European Commission as the latter carries out its duty to guard the Internal Market.

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48 This was set up in 1996 https://www.ombudsman.europa.eu/en/european-network-of-ombudsmen/about/en accessed on 20th March 2024. The European Committee of Petitions is even included in this network.

49 "When redress should have been provided, however, closing the case with a critical remark signals a triple *failure*. The complainant has failed to obtain satisfaction; the institution concerned has failed to put the maladministration right; and the Ombudsman has failed to persuade the institution concerned to alter its position". *The European Ombudsman Follow-Up to Critical and further Remarks how the EU Institutions responded to the Ombudsman's Recommendations in 2008* 5 https://www.ombudsman.europa.eu/pdf/en/4423 accessed on 20th March 2024.

3 Concluding Observations

The European Ombudsman's connection with the European Internal Market is indirect yet continuous. It is 'indirect' in the sense that the European Commission is the immediate guardian and overseer of the European Internal Market, while the European Ombudsman's relationship is with the European Commission, continuously prompting it to carry out its duties beyond its strict legal obligations and into the realm of justice, fairness and correctness. It has resulted from the European Ombudsman's work that it cannot be taken as a given that the European Commission will always execute its duties in a shortcoming-free manner: as we have seen in 2.1 above, European Commission officials had put their gains first and allowed themselves to be lured into the private sector when – no matter what the written rules stated at the time – they should not have been so lured; people have also acted on passion where their favourite football and basketball clubs were concerned to the point of even compromising their duties, they have even been subjected to influence by powerful lobby groups and not taken sufficient steps to protect themselves against this onslaught, they had even failed to take minutes when such minute-taking was crucial. These instances occurred when they should not have; they were also committed by people in high office who are compensated handsomely for their work and thus were even more obliged to know better, but the stark reality is that there is no reason to doubt the real risk that such shortcomings will continue to occur in future and must be guarded against.

Underlying every system is a need to operate not only in line with the written Law but also correctly and diligently encompasses something wider than the written law. This wider concept of correctness and diligence, together with respecting the written Law and established legal principles, is what the European Ombudsman has laid out in the Code of Good Administrative Behaviour and requires from the European Commission. At the same time, it executes its job as guardian and overseer of the European Internal Market. Successive incumbent European Ombudsmen have, since the mid-1990s, worked hard and creatively to continuously prompt the European Commission to do its duty in a fair, well-meaning, altruistic manner for the greater good, for the further growth and strengthening of the European Single Market.

The European Ombudsman's work cannot stop, and whoever holds this prestigious position now and in future cannot rest on their laurels but must sustain and, indeed, where possible, increase efforts to keep the European Commission on its toes, urging it to put right any wrongs committed, always to perform better, to strive to outdo itself and to rise in stature as a result of its increased legitimacy, for the ultimate benefit of the European Citizen, not as a favour or as some concession but because the European Citizen actually finances the

European institutions not least the European Commission through their taxes, and therefore the **paying** European Citizen deserves no less.

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CHAPTER 3

Lost in Translation – Legal Certainty in the EU's Internal Market

Ivan Sammut

Abstract

In this chapter, the author explores the role which translation of legal texts plays as a tool of harmonisation and the techniques involved in securing uniformity between texts, which uniformity is vital to ensure legal certainty.

1 Introduction

Sometimes, it may be argued that multilingualism in the European Union (EU) or legal translation could hinder the functioning of the EU's Internal Market due to discrepancies from translating one language version to another. However, the EU cannot function as an Internal Market without multilingualism. Subsequently, this paper seeks to argue that legal translation is an inherent element of legal harmonisation, intrinsically connected to the very foundations of the EU. Therefore, it cannot be an obstacle. Therefore, this paper investigates how and to what extent EU legal translation contributes to achieving legal harmonisation in the EU. The arguments presented seek to show that EU legal translation is one link in the chain that strengthens the overall success of European harmonisation, contributing to this ongoing debate. However, this research is by no means exhaustive. Not least because the EU is ever-evolving, and so are academic contributions to this debate.

2 Lost in Translation – Legal Translation in the EU's Multi-cultural Environment

"Legal Translation is not Transcoding, i.e. substituting words and phrases of the source legal system by the corresponding expressions of the target legal

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system".[1] The basic unit of translation is not the word but the concept. This is particularly true in the case of the EU, which currently has twenty-four language versions. Council Regulation 1/1958/EEC stipulates that once a language is recognised as official, according to Articles 2 and 4 of the same Regulation, the EU Institutions must communicate with citizens and enact legislation in all the recognised official languages. This includes the legislative instruments adopted for legal harmonisation. Legal harmonisation is the process by which national laws are brought closer to each other for the better functioning of the Internal Market.[2] This is mainly done through EU directives. Hence, the multilingual nature of EU law is inherently linked to the need for uniform interpretation and application of EU law. When Malta, the EU's smallest Member State, joined the EU in 2004, Maltese became the official and the national language, one of two languages, the other being English, in which law in Malta is enforced and implemented. Through Regulation 1/1958/EEC, Maltese had to become an official language of the EU. All languages in national law must become an official EU language. EU law is *de facto* national law, interpreted and applied in the national courts, so EU law needs to be in the same language/s as national law.

EU legal translation contributes to the harmonisation of EU law and the evolution of the European legal culture. The Court of Justice of the European Union (CJEU) has regularly clarified that a uniform interpretation and application of EU law entails uniformity of all the language versions in which EU law exists. In fact, in numerous judgments, the CJEU has emphasised that the need for the uniform interpretation and application of EU law entails that EU legislation must be interpreted and applied "in the light of the versions in all … Languages" (Case 29/69 *Stauder* [1969][3] and more recently, Case C-375/07 *Heuschen & Schroff* [2008].[4] In the *Regina v. Bouchereau* case in 1977, the CJEU added that "the different language versions … must be given a uniform interpretation" (Case 30/77 *Regina v. Bouchereau* [1977].[5]

Thus, the Court makes it clear that while the EU Institutions operate in various legal cultures and languages, institutional multilingualism must still result in the uniform interpretation of the law.[6] Legal harmonisation is the

1 Šarčević, S. (1997), *New Approaches to Legal Translation*, Kluwer: The Hague 229.

2 Baaij, C.J.W. (2012), *The Role of Legal Translation in Legal Harmonisation*, Wolters Kluwer: The Hague 2.

3 ECR 419, para. 3.

4 ECR I-8691, para. 46.

5 ECR 1999, para. 14.

6 Šarčević, S. (ed.) (2015), *Language and Culture in EU law – Multidisciplinary Perspectives*, Ashgate: Surrey 3.

process of using directives, and the EU instructs the Member States to bring their national laws within the parameters set by the Directive. The national laws are written in the official language/s of the Member States, and EU law also requires directives to be available as the authentic version in the official language of the Member State. EU legal translation is not just a 'standard' legal translation from one Source Language (SL) to another; it requires introducing new legal and linguistic concepts. 'New' means this legal culture is created specifically for the EU legal order. As Šarčević's earlier work points out, a proper legal translation is not just being faithful to the text but also recreating the spirit of the text.[7] In the translation of EU legal texts, one can argue that Šarčević's observation can be taken even further, as the legal translator needs to recreate not necessarily the spirit of the Target Language (TL) but must contribute to the creation of a 'new' European legal translation.

Multilingualism is the greatest challenge in EU law, and the paradoxical role of legal translation is very evident.[8] On the one hand, translation is essential for the functioning of EU law as it enables the production of equally authentic texts of EU legislation. On the other hand, legal translation may be seen as inherently imperfect and a potential obstacle to the very goal of legal harmonisation. In the quest for a better translation, which makes up 23 of the 24 authentic linguistic versions, the EU tries to improve the quality of the basic texts of EU legislation.[9] In 2009, DGT launched a *Programme for Quality Management in Translation* (European Commission 2009).[10] At this stage, it makes sense to outline what makes EU translation unique from the perspective of legal translation studies.

There is growing awareness of the inherent link between law, language and culture. This has resulted in greater interaction between lawyers and linguists. Legal Translation Studies is a truly disciplinary field that borrows from translation theory, the theory of law, comparative law and comparative legal drafting.[11] Like in other areas of translation, the legal translator's basic tasks are to

7 Šarčević, S. (1997), *New Approaches to Legal Translation*, Kluwer: The Hague 229.

8 Kjaer, A., 'Theortical Aspects of Legal Translation in the EU: The Paradoxical Relationship beween Language, Translation and the Autonomy of EU Law in Šarčević, S. (ed.) (2015), *Language and Culture in EU law – Multidisciplinary Perspectives*, Ashgate: Surrey, 91.

9 Šarčević S., 'Coping with the Challenges of Legal Translation in Harmonisation' in in Baaij, C.J.W. (ed.) (2012), *The Role of Legal Translation in Legal Harmonisation*, Wolters Kluwer: The Hague 84.

10 ec.europa.eu/dgs/translation/publications/studies/quality-management_translation_en.pdf last accessed on 10th September 2020.

11 Šarčević S., 'Coping with the Challenges of Legal Translation in Harmonisation' in Baaij, C.J.W. (ed.) (2012), *The Role of Legal Translation in Legal Harmonisation*, Wolters Kluwer: The Hague, 84.

translate texts anchored in a specific legal context and intended for a specific purpose or *skopos*, as it is often called in Translation Studies. Normally, this is a dual operation involving an SL and a source legal system with a TL and a target legal system. EU legal translation is more complex, but one must remember that EU law is considered an independent supranational legal system with its autonomous conceptual system.

In this sense, Professor De Groot[12] remarked that the translation of EU texts might be 'relatively easy' because equivalents for EU legal concepts exist in all the official languages. However, one can disagree and argue that this is a narrow approach given that most EU concepts are borrowed from several national systems, international law, and legal transplants, and their linguistic terminology acquires an autonomous EU meaning. One can refer to Anna Lise Kjaer,[13] who said that legal translation in the EU is neither within one legal system nor across legal systems. She argues that EU translation is so complex that it requires "theoretical categories of its own", which consider the special characteristics of multilingual law-making in the EU to which traditional concepts of translation theory may no longer apply.

Regarding translation in EU legal harmonisation, it is necessary to identify the text producers and the receivers in the unique multi-level harmonisation process. EU legal instruments (Regulations and Directives) are produced and adopted by the EU institutions. The former are directly applicable and enforceable in all the Member States, while the latter would need to be transposed into the laws of the Member States. These two levels of governance (the EU and the Member State levels) bring about a corresponding two-step translation process: inter-lingual at the EU level but intra-lingual at the national level.[14] The two steps are inseparably linked and mutually dependent on each other. EU translators need to consider both phases when selecting an appropriate translation strategy. These legal instruments are normally drafted in English or French at the EU level. After the Legal Service approves, they are translated into the other twenty-three languages. The second phase of harmonisation in the case of Directives takes place at the Member State level. At this point, the normally

12 De Groot, G., 'The Influence of Problems of Legal Translation on Comparative Law Research', in Baaij C.J.W. (ed.) (2012), *The Role of Legal Translation in Legal Harmonisation*, Wolters Kluwer: The Hague, 20.

13 Kjaer, A., 'Theortical Aspects of Legal Translation in the EU: The Paradoxical Relationship beween Language, Translation and the Autonomy of EU Law in Šarčević, S. (ed.) (2015), *Language and Culture in EU law – Multidisciplinary Perspectives*, Ashgate: Surrey, 91.

14 Kjaer, A., 'Theortical Aspects of Legal Translation in the EU: The Paradoxical Relationship beween Language, Translation and the Autonomy of EU Law in Šarčević, S. (ed.) (2015), *Language and Culture in EU law – Multidisciplinary Perspectives*, Ashgate: Surrey, 97.

translated version of the language of the particular Member State is taken to draft the transposing local legislation. At this point, the EU linguistic concepts meet with the national linguistic concepts. If there are variations or neologisms, the challenge of integration into national law would be even more demanding.

From the above, one can argue that one of the greatest challenges of legal translation in the EU harmonisation of laws is for translators to produce a Target Test that reads like an original yet preserves good inter-lingual concordance to prevent unintended ambiguity and misinterpretations.[15] One can say that the paradoxical relationship between language, translation and the autonomy of EU law strengthens the argument that EU law mirrors the *sui generis* nature of the European legal order. One can agree with Anne Lise Kjaer,[16] who argues that it is a challenge for practitioners of legal translation and calls for reflection on the part of translation scholars and lawyer linguists. She rightly argues that the real challenge in European law is not a translation in the narrow sense of the word but translation in a broader sociological sense, that is, the transfer of the legal knowledge which is produced and developed by the interaction of lawyers and judges in the European institutions and at the European Courts as participants of discourse communities at the supranational level of the EU law. At the central level, the actors may agree on the 'semantics' of the emerging European law and declare its 'semantic' independence from national law.

However, stating autonomy does not automatically result in autonomy. It still depends on the interpreter's application of the text. Nevertheless, stating the autonomy of European legal concepts does mark a shift in the legal discourse of European lawyers, also at a national level, and discourse can change what people believe is real. When European concepts are constructed as autonomous, people will increasingly treat them as such. Hence, from this argument, one can appreciate the nature of EU legal translation and its contribution to the harmonisation of law in the Internal Market.

3 Legal Certainty – Form and Substance

Legal certainty is a general principle of EU law. Formal legal certainty implies that laws and adjudication must be predictable. Laws must satisfy the imperatives of clarity, stability, intelligibility, and predictability so that those concerned can accurately calculate the legal consequences of their actions and

15 *Ibid.*, 105.
16 *Ibid.*, 105.

the outcome of legal proceedings.[17] Substantive legal certainty is related to the rational acceptability of judicial decision-making. It is not sufficient that laws are predictable. They must be accepted by the legal community in question. Legal certainty encompassing its formal and substantive elements forms an important principle in national legal systems. While principles and the national legal system do not apply automatically to EU law, one would also accept that EU law being enforced alongside pure domestic law will have similar principles. Law requires a certain degree of predictability so that those concerned can know the legal consequences of their actions in advance. The principle of legal certainty comprises a wide concept essential in EU law and the European Union's legal systems. It is the ultimate necessity for the law to be clear, stable, and intelligible.

Therefore, transparency and legitimacy are seen as driving forces behind multilingualism and are closely connected to legal certainty and legitimacy. This is not so much formal validity of the legal system as substantive act ability intertwined with legitimacy. On the one hand, established law guarantees enforcement of legally accepted behaviour and the certainty of law. On the other hand, rational procedures for making and applying the law and a guarantee of legitimate expectations. Law stabilises societal behavioural expectations to create legal certainty that enables law addressees to calculate the legal consequences of their behaviour and those of others. Consequently, legal norms must assume a comprehensible, consistent, and precise form and be made public and known to all addressees. They may not claim retroactivity, and they must govern the factual circumstances in general terms and connect the factual situation with legal consequences so that it is possible to apply the normal to all persons and to comparable cases in the same way.[18]

The concepts of legal certainty and the rule of law are closely connected. The notion of legal certainty is generally used in similar systems. The closest equivalent in common law appears to be the rule of law. Thus, because of its immediate connection to the concept of legal certainty, it is necessary to sketch the basic tenets of all law principles governing the power of authorities. In normative terms, the rule of law refers to the characteristics of an ideal legal system. However, irrespective of the legal system in which the rule of law is virtual, at least one point exists on which there is broad agreement, and the principle escapes any precise definition. The imperatives associated with the

17 Paunio E., *Legal Certainty in Multilingual EU, Language, Discourse, and reasoning at the European Court of Justice,* Ashgate, Surrey, 51.

18 *Ibid*., 52.

rule of law, especially clarity, require that indeterminacy, such as vagueness and ambiguity, be avoided.

Nevertheless, this initialises the following question: how can this view be reconciled with the reality of EU law drafted in over twenty languages, or more accurately, translated into many languages which can carry different views about the meaning of law? How does this work in the multilingual legal system? Accordingly, judicial reasoning must satisfy conditions of rationality and reasonableness. This means that reasons must accompany assertions, and whatever is asserted may be challenged as long as reasons are offered to justify such a claim.[19]

The rule of law forms a building block of any legal system, including that of the EU. Indeed, this is expressed in Article 2 TEU, in which the Union is founded on the values of respect for human dignity, freedom, democracy, equality, the rule of law and respect for human rights. In essence, the rule of law depends on the idea that laws, preannounced rules that govern behaviour in a given legal system, are determinate. Nevertheless, at the same time, the rule of law requires that people can challenge cases laid against this; therefore, it requires stability and flexibility. Again, this relates to multilingualism and legal certainty. If the organising principle is accepted as the guideline for constructing the ideal of the rule of law, then multilingualism and differences between language versions may be acceptable. As long as multilingual EU law is not to wake or not to easily be changeable, it does fulfil the requirement of the rule of law, which is the capacity to guide behaviour. In essence, it has to remain predictable enough; complementing this relativist theory of certainty, it is imperative that those subject to the law must be capable of challenging acts that concern them. This brings about the essential role of the European Court of Justice in harmonising and legal translation.

4 Harmonisation and Legal Translation at the CJEU

Term harmonisation is an essential requirement of any terminological activity. Multilingual terminology harmonisation implies the establishment of equivalences across languages. In several of her works, Sarcevic discusses the problem of conceptual incongruence between different legal systems, which in EU multilingual terminology can be identified as a problem of conceptual mismatching and suggests the need for thorough conceptual analysis as a starting

19 *Ibid.*, 57.

point for determining the adequacy of potential equivalents.[20] EU concepts are often intentionally vague in order to facilitate their application in the different legal and political systems of the Member States. Hence, it is important to improve terminological precision, which may be lacking in some instances. While EU law presupposes the existence of the autonomy of EU concepts, *de facto,* this is an ongoing process, and one can safely conclude that the autonomy of EU concepts is a work in progress. The same official language may be used in more than one state; hence, it is used across more than one legal system, making the possibility of quite complex variations within the same language itself. Naturally, this means that conceptual variability may exist at all levels.

Terminological inconsistencies in the translation of the *acquis* (the body of EU law) occur at the level of the term when different terms are used in the TL to designate the same EU concept, as well as the level of the concept when the term used in the TL is linked to more than one concept, either at EU level or on EU and national levels. To address these issues, creating specific translation tools that enable translators to have points of reference is essential. This brings up the subject of corpora. Vast amounts of documents are constantly translated and made available online. Some examples of large-scale corpus-based linguistic research have produced a parallel corpus on European Parliamentary Proceedings for Machine Translation, a representative parallel corpus of the *acquis* and multilingual text mining and news-gathering tools leading to the creation of the EU's terminology management system designated Interactive Terminology for Europe (IATE).[21]

One can easily identify IATE as a leading corpora concerning EU texts from the above. The various departments of DGs of the European Commission produce EU documents. These documents are usually drafted in English or French. As the writer of these documents is often a non-native speaker of the drafting language, he/she must have access to the terminology used for consultation. Hence, accessing previous texts, particularly the terminology used, is essential to drafting the Source Text. Furthermore, as the Source Text is translated into twenty-three different Target Texts, translators need access to the same corpora the original drafter would have had. As IATE is a parallel corpus, the translator could simultaneously compare the languages used in the Source

20 Sarcevic S., 'Coping with the Challenges of Legal Translation in Harmonisation' in Baaij C.J.W. (ed.) (2012), *The Role of Legal Translation in Legal Harmonisation,* Wolters Kluwer, 203.

21 Murphy A., 'Corpus Analysis of European Union documents' in *Encyclopaedia of Applied Linguistics: Corpus Linguistics,* C. Chapelle (ed.) (2014), Wiley-Blackwell, Oxford, 139.

Language and those used in the Target Language, thus ensuring a smooth and accurate translation.

IATE results are based on input from various groups working at different production levels (drafting) and translating EU texts. If the words are entered into the database by an individual, they are marked with one or two stars depending on the individual's grade. If they are inputted by a Head of Unit, they carry three stars; if they are fields inputted upon by an inter-institutional agreement, they are ranked four stars. This means that words and terminologies carrying four stars result from consultations and agreements by the respective authorities. Hence, the terminology in question carries enough weight to be used in subsequent texts. IATE is more than just a bank of terminology. It has the function of a bank of language as it enables a study of how words and terminology are used in that particular language. It is also much more than a bank of a language as it is available in twenty-four different languages and assists in translating and establishing terminology across policies that fall under EU competence. As stars mark inputs, they serve as a tool for various players to contribute to the linguistic issues of their language without compromising decisions taken at a higher level.

Nowadays, most EU drafting of documents and their translation is made by reference to the corpus. The EU corpora, including IATE, embody most of the different types of corpus mentioned in the introduction of this essay. IATE is a specialised corpus that can be used for specific fields, such as competition policy or environmental policy, and a general corpus of many types. It can be used to compare corpora and teach language.[22] Many EU legal translators study another foreign language during their careers, and IATE is a good tool for learning new terminology and constructing specific language for specific types of documents. Hence, IATE also serves as a learner corpus. As IATE has become larger and more diverse, it is frequently used to make definitive statements about how the language is used. The bigger it grows, the more authoritative it becomes as it assumes more of a representative nature and permanence. IATE is not a mere text collection but is designed to help users understand how certain terminology has gradually been accepted and how this has been mirrored in the chosen Target Language. The IATE interface enables users to search words or phrases through concordance lines.

Most EU documents and legislation are drafted along pre-established templates. Some text parts are standard form templates with little (such as the date or place) or no variation. Then, the majority of the body of the text requires

22 Hunston S., (2002), *Corpora in applied Linguistics*, Cambridge University Press, 12.

the drafter to create the text. However, unlike free literature, while the writer creates the text, he/she is bound by pre-established terminology. This includes proper names of legislation, places or institutions, and predetermined terminology. There may be some words that, in normal language, may be accepted as interchangeable. One can mention 'court jurisprudence' and 'case law' as examples. IATE helps the drafter choose the appropriate wording that fits the sequence of the document. While in a stand-alone translation, any of the two terminologies mentioned above can fit, if the document is part of a sequence, then a drafter has to follow the predetermined choice to ensure consistency even if he/she thinks his choice is better. Without corpora, such as IATE, such a task would be impossible.

The same principle applies to translating the same text into the Target Language. The translator has two important roles that cannot be fulfilled without corpora. The first, as in the case of the drafter in the previous paragraphs, is to fulfil the same task of choosing consistent terminology that respects the type and use of the document. Secondly, suppose the translator works in a new language such as Estonian or Maltese. In that case, the translator is responsible for carefully choosing the appropriate terminology and contributing to developing terminology in his/her target language. Hence, one must ensure consistent terminology in the mentioned Target Language if translating from English into Maltese. However, it may well be that no terminology exists in the target language. In this sense, IATE helps the translator understand how the term is used in the Source Language. Then, one can do a comparative exercise in another more established language (established in the sense of EU terminology), such as Italian. Having studied the use of words in Italian, one can then make choices for the Maltese version. Eventually, such choices may be entered into IATE itself, expanding the corpus in the Target Language and assisting future translators of similar texts. While corpora are useful, one should look at linguistic concerns while translating EU law.

Legal translation in a multilingual environment is not only a linguistic undertaking but may have direct legal consequences caused by faulty translation. A good example of possible faulty translation has been addressed by the CJEU in Case C-54/05 *Commission V Finland* ([2006] ECR I-02473), where the Court explains:

> Although the Finnish version of that provision contains no reference to the requirement that overheads are allocated 'pro rata' to the operation in question, the fact is of no consequence, since it follows from settled case-law that Community provisions must be interpreted and applied uniformly in the light of the versions existing in all Community languages

> and since, in this case, the language versions other than Finnish expressly refer to the requirement that overheads be allocated pro rata or proportionately to the operation in question.

The challenge for legal translation brought about by the above judgment is how to mix linguistically and legally different national legal cultures and that of the EU and maintain coherence. Even in one of the old landmark cases dealing with the general principle of human rights, the CJEU in *Stauder* ([1969] ECR I-419) said that for the sake of uniform interpretation, it was impossible to consider one version of the text in isolation. At that time, only four official languages were spoken. Hence, one can say that the experience of EU translation today may go beyond multilingualism and into the concept of plurilingualism.

The above can be taken as an argument whereby legal translation requires understanding the deeper level of legal language, which may be called the legal-epistemic level. In the past, Europe's legal language was Latin. Today, English may be regarded as a technical *lingua franca,* although there are problems associated with this.[23] The main problem is that some jurisdictions may still prefer other languages, such as Latin.[24] Considering EU law, one realises that around 90% of legislative documents are drafted in English. The rest is almost translated into English immediately, and stakeholders, eurocrats and translators are more likely to use the English version, given that it is the main working language. If English is not the drafting language, the English version will still likely be the main bridge to translate into other languages. Hence, is it safe to answer the question of what language law speaks? The answer is English. Therefore, one can conclude that English is the main language for drafting and translation as it would probably be a Source Language if not a Target Language.

In the past decades, the spread of English has received considerable attention among scholars of the English language. The case of English in the EU is no exception. It is a new variety of English with its special jargon, even if the existence of a specifically European variety of English as a *lingua franca* is far from being widely acknowledged. Some writers use 'Euro-English' as opposed to 'EU English' as described below. These terms refer to English as a *lingua franca* in the European context. As Modiano points out, Euro-English brings non-native speakers of English into contact with other non-native speakers in Europe, even more perhaps than native speakers. As a result of

23 Pozzo B., 'English as Lingua Franca in the EU Multilingual Context' in Baaij C.J.W. (ed.) (2012), *The Role of Legal Translation in Legal Harmonisation,* Wolters Kluwer, 184.

24 *Ibid*., 201.

this phenomenon, one can notice the emergence of typical lexical choices, discourse strategies and even accents that can be studied if Euro-English is to be accepted as a linguistic reality.

Contrary to Euro-English, which can be described as a non-native variety of English, often used in drafting documents mainly by non-native speakers, EU English is produced by native speakers of English since it is produced by linguists whose English is the first language. When a particular text is originally drafted in another language, this is translated by the English unit of DGT, who are, as per employment requirements, native speakers of English. Research projects focusing on EU English have investigated lexical features with the help of corpora of the EU, mainly legal documents.

EU English deals with various activities in which the EU is involved. Reference can be made to the work of Trebits in her article *English for Specific Purpose,*[25] who studied the use of English in the recruitment competitions organised by the European Personnel Selection Office (EPSO) and compared the results with the Corpus of EU English (CEUE). All the texts in the CEUE were published after 2000, and the final version contained over 200,000 running words. This corpus may appear small but valid as it is highly specialised and limited. She compared the results with the written part of the British National Corpus (BNC) using lexical frequency and range computer programs. The frequency list allowed her to draw up the list of the most frequent conjunctions in the CEUE and compare the two corpora in terms of categorises of the conjunctions used.

Another corpus-driven study by Jablonkai Reka was published in the Journal *English for Specific Purpose*, where she identified and analysed lexical bundles in written English EU discourse using the corpora mentioned above. She concluded that English EU discourse differs from other written registers in several aspects.[26] First, she observes that EU texts use bundles with verb phrases more. Secondly, lexical bundles appear in fairly high frequencies. Hence, the corpus suggests that most EU texts consist of formulaic patterns. The different nature of the lexical bundles in written English EU discourse is important to raise awareness of the difference between English used for EU purposes and general English. Reka's study shows that the use of English in European affairs has developed in a special way to fit its purpose, and this comes out clearly when one looks at the various applicable corpora. In her study, she concludes

25 Trebits A., 'Conjunctive cohesion in English language EU documents – A corpus-based analysis and its implications', *English for Specific Purpose* 28 (2009), 204.

26 Reka J., 'English in the context of European integration: A corpus-driven analysis of lexical bundles in English EU documents' *English for Specific Purpose* 29 (2010) 253–267.

that corpora-driven research about the use of English in EU texts provides a coherent picture of the lingua franca's use within an EU context for courses and materials designed to teach English for EU purposes.

Turning back to the problems of legal translation, every comparative lawyer is a translator, as language is central to acquiring knowledge of foreign law.[27] The complexity of the multilingual situation necessitates European institutions to take the initiative to rationalise the situation, given that EU legal translation needs to navigate among more than 500 possible language combinations from all official EU languages into all official EU languages. They used a lingua franca, even if merely as a point of reference, which will contribute to better uniformity. However, the use of English also presents an additional challenge. The English language necessarily brings with it the ideas of common law. The English used in EU law differs from that used in common law. It is a new language, and its role is quite peculiar. It is just one of twenty-four languages, and EU texts take their meaning from all language versions, which are often drafted and negotiated by non-native speakers. Styles, concepts, and words are taken from other languages and adapted to English. Hence, English in the EU has become a 'neutral' or 'descriptive' language, a reference point for the Eurocrats and the stakeholders. It is a comprehensible language that is not necessarily tied to English law. It is the language from which one can create neologisms. In this context, English is undergoing an evolution.

Most problems relating to translating the Draft Common Frame of Reference (DCFR) and the Communication on European Sales Law (CESL) are apparent when translating this *lingua franca* into all the other official languages. For example, how can one translate French concepts codified in English with a German background? These legal instruments contain agreed or compromised definitions offered by the authors in their commentaries. The appendix to the DCFR has a long list of definitions of the terms used in formulating the rules.[28] In translating standardised English into the other twenty-three languages, if there is no equivalent in the language and the particular context of notions and concepts belonging to the national experience, it will be necessary to create 'new' terms, concepts and principles.

Felici explains how, although English has been used since the EU acceded to what was then the European Economic Community in 1973, the increase in the use of English as a *de facto lingua franca* gathered momentum, first with the Scandinavian enlargement in 1995 and then achieved the current boost with

27 Pozzo B. *op cit.,* 200.

28 Pozzo B. *op cit.,* 200.

the 2004 enlargement.[29] This is supported by the statistics published by the Commission in 2009 (*Translating for a Multilingual Community* (2009), which reports that while English as SL was 72.5% in 2008, fifteen years before, it was 45.4%. French went down from 40.4% to 11.8%. Such a considerable increase in the use of English over a short period inevitably contributed to an unmarked form of English devoid of cultural specificity. Hence, one can find new terms such as *internal market, pigmeat,* etc. Other words or phrases have acquired new meanings due to the influence of other languages. For example, one can mention the *actual* meaning of 'current' or *if it is* used to replace the preposition 'for'. These are just examples, and listing them down is beyond the scope of this work.

One can argue that EU legal English looks more like civil law than a common law style. The EU style guides are closely built on the original French style guide drafted before the UK and Ireland joined the EU. Before this, French was the *de facto lingua franca* among just four official languages. English crept in slowly like an incoming tide up an estuary, and as a result, one can say that we have the anglophonification of the incumbent French style. While English may have replaced French as the *lingua franca*, the same cannot be said about style and terminology. Some new terms or styles come from French, even from the few examples in the preceding paragraph. Hence, it can be argued that Euro-English is, in fact, 'English' in the French way. This may be debatable, but some form of French influence exists.

Felici explains that:[30]

> These semantic changes can be attributed to the multilingual production of EU legislation and to the translation from one language to another during drafting and negotiations, as well as to the need of adapting English to the EU legal context. On the other hand, the first EU English translations were translations from French; hence, both terminology and drafting style are inevitably shaped by the continental legal traditions and Romance language influence.

Thus, multilingualism's next challenge in the EU is translating English into a *lingua franca*. The more English is used, the more challenges may be posed. One may no longer face the problem of transferring legal concepts from one legal

29 Felici A., 'Translating EU Legislation from *Lingua Franca*: Advantages and Disadvantages' in Sarcevic S. (ed.) (2015), *Language and Culture in EU law – Multidisciplinary Perspectives*, Ashgate, Surrey, 126.

30 *Ibid.,* 127.

language into another, but the challenge would be translating from a hybrid language. Hence, a 'common frame' of reference is essential, even for linguistic purposes. Also, while neologisms may be necessary, they create new challenges in their own right, and they would require monitoring, ideally through some form of institutional supervision. A similar approach has been taken in francophone parts of Canada, where legal terminology has been standardised in multiple languages. Is English suitable for the purpose? English is a forced choice in the current circumstances of the EU, and the larger the enlargements, the more essential the use of English becomes as a *lingua franca.* Euro English will develop its path and terminology independently of what the Law Lords think. Euro-English could become a new dialect of English while contributing to achieving the much-sought uniformity in EU law.

From the above, one can conclude that EU legal translation is a special genre in its own right because English as the dominant language renders EU legal translation beyond the normal classification of SL and TL. This results from negotiations and interactions among speakers of different languages, mainly through a language that may not even be their second language. Hence, many authors or drafters from different cultural or linguistic backgrounds may prevent professional translators from identifying the author's clear intention.[31] Text intention is rather influenced by the intercultural communicative process among the Member States, and tests reflect the dynamics of intergovernmental cooperation, resulting in a situation where languages and legal systems are in contact. Going beyond this argument, one can also appreciate that the different EU institutions have different needs. Hence, EU multilingual legislation poses new challenges to translation depending on the genre and function of the legal text and the different institutional needs, making the effect of multilingualism in the EU on European legal translation even more challenging.

5 Conclusion

The central question examined in this paper is how legal translation can contribute to legal harmonisation. The pivotal function of legal translation is one of the most elementary operations of the EU. The EU cannot function without translation. Legal translation is indispensable to harmonise laws to benefit the Internal Market. EU law must be accessible to all EU citizens independently of

31 *Ibid.*, 129.

the language version, so in this sense, legal translation is critical to achieving the objectives of the European Treaties.

As highlighted in this paper, translation to draft the EU's multilingual legislation is a complex legal translation as each language version is considered authentic. As a consequence of this uniformity, the unity of the law must be preserved. Each version must correspond not only linguistically but also in structure and content. Hence, it is the task of the EU legal translators to produce twenty-three accurate and reliable texts with the same meaning. As stated earlier, complete correspondence between the language versions of the EU legislation is essential to harmonise laws. It has also been argued that EU legal translation merits considering a special genre of legal translation as certain skills and techniques are particular to EU legal translation as opposed to legal translation in general.

The real challenge of EU legal translation is not just the lack of uniform terms but also the lack of uniform legal concepts. This means that EU legal translators face the challenge of managing the conjuncture of national and EU legal languages while maintaining sufficient coherence. Thanks to the legal translation process, EU experts can contribute to creating a 'new' European legal culture with autonomous legal concepts. The autonomy of the 'new' European legal culture not only creates a challenge to lawyers but also a new challenge to linguists regarding how to achieve a single legal language in all the official languages. Regarding this challenge, the increasing use of English as a *de facto lingua franca* in which a single legal language contributes to developing a 'new' legal culture is facilitating the achievement of some form of uniformity in EU law.

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CHAPTER 4

The Transformation of European Private Law – Harmonisation, Consolidation, Codification or Chaos?

Ivan Sammut

Abstract

In present-day Europe, the basic nineteenth-century situation where each nation-state had its legal system still prevails. The codes have survived on the European continent, and the nation-states are still strong. The same can be said of uncodified English law, whose hold on England and Wales is still very powerful. While the tools contribute towards the approximation or unification of law, an issue that remains to be discussed is what form the harmonised or unified law should take. Besides the format, one must also look at the law's substantive composition. The answer to this question depends on which tools are used. Harmonisation, even if comprehensive, does not lead to a unified law system, so the nation-state law is preserved as it is, at least in form. The answer to the question also depends on the substantive nature of the Europeanized law, including social, political and perhaps religious values behind the substantive law. Thus, one has to analyse the different fields of private law on their own merits, and the choice of tools may also depend on the field. The author demonstrates what can be achieved with the current mode of governance concerning the development of European Private Law (EPL). From the most recent developments, it can be concluded that Europeanisation is an ongoing process. However, with the current modes of governance, this will likely continue through more fragmentation and in a very limited role, sometimes without even achieving the desired objectives highlighted in the various preambles. As the Internal Market may necessitate the further development of EPL, which current modes of governance do not permit, it is clear that it may be necessary to examine how innovative modes of governance discussed earlier can take the development of EPL further.

1 Introduction

The current debate on European private law's desirability and modes of formation engages many scholars and institutions. Most of the current academic

works in this field concern the search for a common core of European private law, the rationalisation of the *acquis communautaire*, the design of a European Civil Code, and the advantages and disadvantages of the codification of private law or single subject matters.[1] These ongoing projects concerning the challenges faced by the Europeanisation of private law concern the definition of private law underlying the debate about the creation of European private law.[2] Here, the focus is more on whether European private law will eventually evolve into a European Civil Code, whether there is a sufficient legal basis in the EU Treaties, and whether such a code is desirable. When unified law is not possible, harmonisation of private international law rules may be useful to achieve the objectives of the Internal Market. Most of these writings conclude that while a European Civil Code may be desirable for the needs of the Internal Market, it appears to be more of a long-shot than a foreseeable reality.[3] This paper discusses the de-nationalisation of private law in the Internal Market, followed by what was proposed a decade ago. As there has been no major development since then, the paper concludes by charting a possible way forward, at least in the short term.

2 The De-nationalisation of Private Law and the Internal Market

In the age of globalisation, the action of strong political and economic forces, the ease of travel, the development of communication technologies and the advent of the Internet contribute to the convergence of national societies in a shift from territorial to functional differentiation at the world level.[4] The field of law is also becoming 'globalised'. The diverse sectors of the new 'world society' are developing their legal frameworks, thereby displacing the importance of state-produced law and legal centralism. An example of transnationally developed law concerns the field of international trade and finance. Long before the process of globalisation became a reality, there was already the existence of a *lex mercatoria*, a global law of trade and commerce created by merchants themselves, outside the legal monopoly of the State. As a matter of

1 See Grundmann, S., & Schauer, M., *The Architecture of European Codes and Contract Law*, The Hague, Kluwer, 2006, 3.

2 See Hesselink, M. (ed.), *The Politics of a European Civil Code*, The Hague, Kluwer, 2006, 5.

3 See Collins, H., *The European Civil Code—The Way Forward*, Cambridge, 2008, 1.

4 Teubner. G., "Global Bukwina: Legal Pluralism in the World Society", G. Teubner, (ed.) *Global Law Without a State,* Dartmouth, 1997, 3 *et seq.*

fact, "the regulation of trade and commerce has constituted a trans-cultural phenomenon since immemorial".[5]

Parallel to the process of globalisation, another significant phenomenon that erodes the importance of national boundaries and the inception of the State as the centre of the legal order is taking place in certain geographical areas.[6] It is the regional integration process, with a maximum exponent in the European Union. This is witnessing the gradual transformation of European sovereign states into a new political entity without historical precedents, breaking the traditional dualism of states and international organisations. The Member States play a central role in the decision-making process at the European level. However, they do so in a constitutional-legal context which they do not fully control: EU law is gradually developing into an autonomous, distinct and independent supranational legal order, possessing primacy over the law of the Member States, and the provisions of which are directly applicable to the nationals of the Member States.

Originally, the purpose of the then Community was to create a common market whereby the free movement of goods, services, persons, and capital could be guaranteed. In 1985, the Commission published the White Paper' *Completing the Internal Market'*, which proposed an Internal Market whereby the four freedoms are complemented by the suppression of all kinds of physical barriers, technical or fiscal, which hinder the fundamental freedoms or distort competition.[7] Following the Maastricht Treaty, the EC abolished border controls on the movement of goods within the Community as of 1 January 1993. This was a very important step towards creating a real single market. Today, the European Union is an Internal Market without physical control at the internal borders for goods and persons for those Member States who form part of the Schengen area.

The means to achieve the aims of the EU are the progressive approximation of the Member States' economic policies, establishing an Internal Market, following the Maastricht Treaty, and establishing an Economic and Monetary

5 Von Ziegler, A. "Particularities of the Harmonisation and Unification of International Law of Trade and Commerce", J. Basedow, et al *Private Law in International Arena-Liber Amicorum Kurt Sihr*, T.M.C. Asser Press, The Hague, 2000 875 *et seq*., 877.

6 Wilhelmsson. T., "Jack in the Box Theory of European Community Law", Erikson & Hurri (eds.) *Dialectic of Law and Reality*, 1999. p. 437 et seq., 447.

7 Communication from Commission to the Council on the completion of the Internal Market of June 28, 1985, COM (85) 310 final.

Union (EMU). The Court of Justice of the European Union (CJEU) in the *Schul* case explains that establishing a common market entails:[8]

> The elimination of all obstacles to intra-community trade in order to merge the national markets into a single market bringing about conditions as close as possible to those of a genuine Internal Market.

The argument is that the more the four freedoms move freely, the more affluent Europe could become. Free movement involves private law. Anyone doing business across borders knows that a foreign contract law could govern some parts of his contract. The process of achieving a complete Internal Market has not yet been concluded. While the law is an instrument to achieve this goal, it could also act as a barrier if not unified or at least harmonised. The Internal Market has not been complemented by unification, or at least an approximation of contract law among the Member States. The unknown laws of the other Member States are a risk, which could result in an obstacle to achieving the desired Internal Market.[9] A transaction between Marseille and Lille could be less risky than one between London and Lille. The need for a European private law stems from the need to address this issue.

A high degree of harmonisation of the private laws has been achieved based on secondary EU law.[10] For example, European contract law can be analysed from two perspectives. First is a 'Critical Mass of Piecemeal Legislation', and then the Rome Regime. The notion of piecemeal legislation also applies to other forms of private law, such as labour law or company law. During the last four decades, the harmonisation of contract law through EU directives has progressed rapidly. This is particularly true in the case of consumer contract law. For example, one can mention the directives of consumer goods,[11] Late Payments,[12] Electronic Commerce,[13] and Doorstep Selling.[14] Directives

8 Judgement of 5.5.82, in case 15/81, *Schul v. Inspecteur der Invoerrechten en Accijnzen*, [1982] ECR 1409.

9 Lando O., "Some Features of the Law of Contract in the Third Millennium", (2000) 40 *Scandinavian Studies in Law,* 343.

10 Vahrenwald A., "European Contract Law", (2002) *Entertainment Law Review*, 57.

11 European Parliament (EP) and Council Directive 1999/44/EC of May 25, 1999, on certain aspects of the sale of consumer goods and associated guarantees, OJ L 171/12, 7.7.1999.

12 EP and Council Directive 2000/35/EC of June 29, 2000, on combating late payments in commercial transactions, OJ L 200/35, 8.8.2000.

13 EP and Council Directive 2000/31/EC of June 8, 2000, on certain legal aspects of information society services, in particular e-commerce, in the Internal Market, OJ L 171/1, 17.7.2000.

14 Council Directive 85/577/EEC of December 20, 1985 to protect the consumer in respect of contracts negotiated away from business premises, OJ 1985 L372/31.

such as those above often give the Member States a range within which they can adopt measures. This will likely increase the cost of a client seeking advice to do business. Accordingly, it could be argued that only 'unified' legal rules can provide a cost-effective solution.

However, 'unified' legal rules are not always practical. Unless the Internal Market becomes a unified legal system, one would have to provide for national laws that come into operation whenever a national court is faced with a claim that contains a foreign element.[15] In an area of private law where a 'unified' law system is not in place, one would have to resort to conflict of law rules, and therefore, it is important to ensure a certain degree of consistency from this aspect.

The above-quoted directives form part of substantive European contract law. However, a very important instrument governing European contract law is the Rome Regulation[16], previously a Convention of 1980[17], which can be said to form part of European Conflict of Law rules rather than merely substantive contract law. The object of the Regulation is the unification within the Internal Market of the rules relating to the choice of law as applied to contractual situations.[18] The Regulation is used by Member States courts to resolve cases within its material scope where the question arises as to what the appropriate territorial law is to be applied in certain contractual situations. It applies to all such cases whether or not there is any connection with the EU and whether or not the applicable law is that of a Member State. Another important European private international law instrument is the 'Brussels Regulation', a convention before. However, it has now been communicated and updated by the Recast Regulation, which came into force in 2015.[19]

Given the above, an intense debate has arisen on the need to enact comprehensive private law, especially contract legislation at the EU level. The debate has been academic for some time, with an almost non-existent political

15 North P. & Fawcett J., *Cheshire & North's Private International Law*, 13th ed., Butterworths, London, 1999, 3.

16 Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I).

17 1980 Rome Convention on the law applicable to contractual obligations (consolidated version).

18 Williams P.R., "The EEC Convention on the Law Applicable to Contractual Obligations", (1986) 35. *International and Comparative Law Quarterly*, 1.

19 Council Regulation 44/2001EC of December 22, 2000 on jurisdiction and enforcement of judgements in civil and commercial matters, replacing the Brussels Convention of 1968, OJ 1998 C-27, 26.1.1998. & Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (recast).

backup. However, after the European Council held in Tampere in 1999,[20] this issue was installed in the political arena, with various resolutions from the European Parliament and a Communication[21] from the European Commission to the Council and the European Parliament on European Contract law.[22] The Commission came up with the following four alternatives:

i. to leave the solution to any identified problems to the market;
ii. to promote the development of non-binding common contract law principles, useful for contracting parties in drafting their contracts, national courts and arbitrators in their decisions and national legislators when drawing up legislative initiatives;
iii. to review and improve existing EU legislation in the area of contract law to make it more coherent or to adapt it to cover situations not foreseen at the time of adoption;
iv. to adopt a new instrument at the EU level.

3 The Green Paper on Policy Options for Progress Towards a European Contract Law for Consumers and Businesses COM (2010) 348 Final

More than a decade later, in 2010, the European Commission developed a Green Paper on policy options for progress towards a European contract law for consumers and businesses on 1 July 2010.[23] The Commission argues that the Internal Market is built on several contracts governed by different national contract laws. The differences in contract laws may entail additional transaction costs and create legal uncertainty for some transactions. This could lead to a reduction in consumer confidence. Another problem is that national laws are rarely available in other European languages, and therefore, market players may need to seek costly advice from lawyers in other less familiar jurisdictions. As a result, SMEs with limited resources may find it hard to engage in cross-border activities to the detriment of Internal Market building, which is supposed to increase sellers' and consumers' choices and opportunities. The Commission wants citizens to take full advantage of the Internal Market and,

20 Presidency Conclusions, Tampere European Council 15 and 18 October 1999, SI (1999).
21 Resolutions of the EP OJ C 377, December 29 2000, 323.
22 Communication from the Commission to the Council and the EP on European Contract Law of July 11, 2001, COM (2001) 398 final.
23 Green Paper from the Commission Paper on policy options for progress towards a European Contract Law for consumers and business COM (2010) 348 final.

for this reason, wants to ease cross-border transactions. The Green Paper aims to establish how to strengthen such businesses and launch a public consultation. The following are the options proposed.[24]

Option 1	**Publication of the work of a group of experts looking at the issue**
Option 2a Option 2b	a. An official "toolbox" for legislators adopted by the Commission b. An interinstitutional agreement between the Commission, the European Parliament and the Council
Option 3	A Commission Recommendation encouraging Member States to incorporate an instrument of European contract law into their national laws
Option 4	A Regulation setting up an optional instrument of European contract law
Option 5	A Directive on European contract law to harmonise national contract laws based on minimum common standards
Option 6	A Regulation establishing a European contract law to replace national laws with a uniform European set of rules
Option 7	A Regulation establishing a European civil code

Options 1 to 3 are not new in European contract law, as earlier Commission documents have included them.[25] One may argue that the first three options cannot be taken seriously. The Green Paper itself does not seem to favour these three options. Concerning Option 1, the Green Paper remarks that the publication of the work of a group of experts would not address the Internal Market barriers. This Option has little or no value whatsoever. It merely applauds the publication of a document prepared by a selection of experts. It remains to be seen whether or not this aids the realm of European contract law. However, various actors have supported publishing the results, especially since public funds have funded this academic exercise. This publication would supplement the comparative law discussion that has kicked in in this area. It could be

24 *Ibid.*, 2.

25 Commission (EC) European Contract Law and the revision of the acquis: the way forward, (Communication) COM (2004) 651 final, sub 3.2.4 (option 1) and sub 2.1.1 (option 2) and the 2003 Action Plan, COM (2003) 62 final (option 3). In the more recent communications, the recommendation option is no longer mentioned (Second Progress Report from the Commission on the Common Frame of Reference, COM (2007) 447 final).

argued that the Commission has been involved in producing a contract code (disguised as a CRF) for so long that it is now merely eager to publish it. Mere Publication does not take European contract law a step further in any direction but merely strands this movement in a *status quo*.

Option 2 suggests a toolbox. This Option is similar to the position the Council took in its resolution on a more coherent European contract law back in 2003.[26] This offers two possible options: crystallised into one: i) Option 2(a) an official "toolbox" for legislators adopted by the Commission, or ii) Option 2(b) an official "toolbox" for legislators adopted by an inter-institutional agreement between the Commission, the European Parliament and the Council. The latter Option seems *prima facie* attractive. It is not new to the EU agenda. As far back as 2007 and 2008, the Commission used the word "toolbox" to refer to its CFR.[27] However, the Green Paper states that the so-called "toolbox" would "not provide immediate, tangible internal market benefits since it would not remove divergences in law".[28] Just like Option 1, this Option also aims to use the CFR in a non-binding way for both the Member States and their citizens. However, unlike Option 1, Option 2 seems to have been favoured by various respondents, as seen in the Publication of the feasibility study results by the Expert Group on European contract law for stakeholders' and legal practitioners' feedback.[29] This Publication states that Options 2 and 4 were the most favoured options by the respondents. Most respondents only expressed opinions on a toolbox (Option 2) and an optional instrument (Option 4). Out of those respondents who made explicit comments concerning the scope of the toolbox (Option 2), the majority believed it should be as comprehensive as possible, i.e. it should not be restricted to certain types of contract and should have a rather broad scope.

Contrary to Option 1, the "toolbox", as envisaged in Option 2, has also been described as a more official instrument with a formal status. It provides a legal framework for European legislators to use as a reference tool. The scope

26 Council Resolution "On A More Coherent European Contract Law" of 14 October 2003, O.J.2003 C 246/1 where the Council stated that the Common Frame of Reference should not be a legally binding instrument.

27 Commission: Second Progress Report on The Common Frame of Reference, COM (2007) 447 final, 25 July 2007; European Parliament: resolution of 12 December 2007, P6/-TA(2006)0615; Council: statement on 18 April 2008 endorsing Draft report of the Committee on Civil Law Matters to 2008, 8286/08.

28 Commission (EC) Policy options for progress towards a European Contract Law for consumers and businesses, (Green Paper) 1 July 2010, COM (2010) 348 final 8.

29 <http://ec.europa.eu/justice/contract/files/feasibility-study_en.pdf> last accessed on 15 December 2023.

behind this framework is to ensure coherence and quality of future legislation and to prevent different understandings of terminology at the EU level, such as the definition of a consumer. This Option proposes three ways a "toolbox" could be created: a decision, a communication or an interinstitutional agreement. The latter two do not require a specific legal basis. A decision would, however, require this since it is a legislative act. Adopting the toolbox as a communication or decision does not have the potential to achieve the Commission's goals. However, a remedy for this Option is possible should the EU adopt this instrument through an interinstitutional agreement since an interinstitutional agreement binds the three institutions that constitute the European legislature. Option 3 suggests using a Commission Recommendation, which encourages Member States to incorporate an instrument of European contract law into their national laws. A recommendation would not have any binding effect on Member States, so Europe will not benefit from this in terms of harmonisation, especially since it bears the risk of an incoherent and incomplete approach between the Member States.[30] This Option may also be subdivided into two options, although the Green Paper does not divide it as such. First, the possibility of a recommendation encourages Member States to substitute national contract laws with the recommended European instrument. Secondly, a Commission recommendation will encourage Member States to incorporate the European contract law instrument as an optional regime, offering contractual parties an alternative to national law.

Concerning this Option, the Green Paper also refers to the United States; however, the United States' experience cannot be compared to the European one. This is because the EU Member States differ so much that this comparison cannot be made. Furthermore, the EU has twenty-four different languages, whereas the USA has one shared language.[31] One can note that the first recommendation would encourage the complete replacement of national contract laws with European contract law. In contrast, the second form would encourage national legislators to provide an alternative to national law by accepting an optional instrument of European contract law. The second recommendation, dealing with the availability of an alternative to national law from a replacement of national law, has been favoured. A substantive choice of law that runs in parallel with domestic law could be economically and legally desirable from a competitive point of view since "plurality offers more choices,

30 Cartwright, J., "Choice is Good. Really?" *European Review of Contract Law*, 2011, Volume 7, Issue 2, 335–349.

31 Commission (EC) Policy options for progress towards a European Contract Law for consumers and businesses, (Green Paper) 1 July 2010, COM (2010) 348 final 8.

legal systems should compete".[32] An optional instrument would lead to fewer problems from a constitutional perspective. This aspect shall also be dealt with relating to Options 4, 6, and 7, and it will also bring about less conflict in terms of a legal base.

Furthermore, one cannot forget that the market is the transaction leader. More legitimacy can be achieved if the market resorts to the optional instrument. This Option includes a particular feature shared by Options 1 and 2 but not imposed upon the parties. On the contrary, the parties may autonomously select the instrument to apply as their regime.

However, the alternative nature of the Regulation and its non-binding nature may also prove problematic, especially since this would mean that it would only be a recommendation to the Member States, and convergence would remain dependent on the willingness of the Member States. Furthermore, the lack of any "push factor" may delay applying an optional instrument. It is for this reason that many working groups have opined that a recommendation would be insufficient to encourage parties to conclude agreements under the same set of provisions within the entire Union, especially as Member States have the option to take on the recommendation differently and at different moments in time or not at all.

In terms of effectiveness and desirability, all three options suggest that the existing Draft Common Frame of Reference (DCFR) is turned into a type of "soft law" which would allow the EU as well as the Member States to refer to the DCFR when it comes to drafting future contract law. Then again, if the CFR is published following Options 2 and 3, it would not merely mean that the *status quo* is retained. On the contrary, the DCFR would pick up further momentum because it would be published in the Official Journal. It would have to be made available in all twenty-four official languages of the EU (whereas, at the moment, it is only available in English), and it would bear the "official stamp" of the EU. This would allow courts and lawmakers to resort to the CFR since it is more available.

This means that although Options 1–3 are, in reality, non-binding, they still carry a certain degree of legal effect. The Max Planck Institute has described them as an attempt to codify European contract law through the back door. All these options may and are intended to lead to a creeping harmonisation of national contract laws.[33] Nevertheless, how far these "soft-law" instruments

32 Kerber, W., and Grundmann, S. "An Optional European Contract Law Code: Advantages and Disadvantages", *Eur J Law Econ* 2006, 21.

33 Basedow, J., et al. *Policy Options for Progress towards a European Contract Law: Comments on the Issues Raised in the Green Paper from the Commission of 1 July 2010, COM*

may achieve the goals that not even "hard law" instruments can achieve remains dubious. The non-binding nature of Options 1 to 3 is not what Europe needs now. In addition to these options, the Green Paper proposes a set of three other options, namely Option 5 to 7—Option 4, which is the most favoured Option by most parties, sits in the middle.

In contrast to Options 1–3, these Options have a binding effect upon the Member States, although the binding effect of these instruments varies. These options are "hard law" since they would approximate the Member States' contract laws if Option 5 is adopted. In contrast, they would replace the Member States' contract laws with a European set of rules if Option 6 or 7 is adopted. These Options and Option 4 greatly affect several transactions, so legal certainty on a legal basis should be guaranteed. Due to a lack of competence, European Contract Law cannot afford to be challenged before the CJEU. The Commission erroneously omits considering the legal basis for these "hard law" instruments. This is unacceptable. As mentioned earlier, the Treaties do not provide an explicit legal basis for harmonising contract law. Nor do they provide one for private law. Hence, whether the EU can adopt the Options suggested in Options 6 and 7 remains dubious.

Option 5 suggests the adoption of a directive setting out minimum common standards for contract law. This would leave significant differences in national laws and achieve nothing except grief for those seeking to negotiate those minimum standards.[34] It is also hard to believe that EU member states are yet ready to abandon their national contract laws, let alone the entirety of their civil laws, in favour of a single European law, even if the EU had the power to create a single European law. A Union that is committed to allowing a choice of law in contractual relations, to freedom of contract in business dealings, to respect its "rich cultural and linguistic diversity", to safeguarding and enhancing its cultural heritage and to subsidiarity and proportionality cannot rationally impose a legal monoculture on all of its members.[35] This Directive would harmonise national contract law by providing a set of minimum common standards which the national legislator would be expected to adopt.

(2010) *348 final* (January 27, 2011), Rabels Zeitschrift für ausländisches und internationales Privatrecht, Vol. 75, pp. 371–438, 2011; Max Planck Private Law Research Paper No. 11/2. Available at SSRN: http://ssrn.com/abstract=1752985 last accessed on 15 December 2023.

34 Commission (EC) Policy options for progress towards a European Contract Law for consumers and businesses, (Green Paper) 1 July 2010, COM (2010) 348 final 10–11.

35 See Cartwright, J., "Choice is Good. Really?" *European Review of Contract Law*, 2011, Volume 7, Issue 2, 335–349.

This Option has, however, been refused on four main grounds:

I. First, implementing the Directive would bring about added costs, especially since it foresees minimum harmonisation.
II. Secondly, minimum harmonisation does not provide a uniform transposition and interpretation of rules.
III. Thirdly, since the domestic laws would still be in place, conflicts would arise in drafting these cross-border instruments, especially since most parties would not be acquainted with the new instrument.
IV. Fourthly, businesses would have to make considerable investments to adjust contract law.

These minimum common standards would bring about what has been referred to as a legal monoculture within the EU. This could drive offshore international legal work that previously operated under a domestic regime, which is hardly good for Europe. Furthermore, Option 5 is also recognised as capable of achieving the Commission's aims and running the risk of interfering with the Internal Market rather than improving it. This is mainly attributable to the Directive being a minimum harmonisation directive. In its review of consumer acquisition, the Green Paper also refers to these issues. Unsurprisingly, Option 5 is not recommended since it could never give Europe the comprehensive European contract law it is looking for and would thus complement neither the Internal Market nor its participants.

Option 6 proposes a Regulation establishing a European contract law which, according to the Green Paper, could raise sensitive issues of subsidiarity and proportionality. It has also been described as avoiding the downsides of Options 5 and 7. This option suggests fully harmonising contract laws by enacting a uniform contract law regime to eliminate all national and domestic deviations. However, this approach must be studied carefully, especially since one cannot underestimate the difficulties resulting from interpretation. A uniform law in all Member States would not necessarily mean that a common interpretation would be attributed throughout all these territories. This role would be attributed to the CJEU, yet the domestic interpretation of provisions can never be eliminated.[36] This option is directly applicable and also binding on Member States. This would imply that it would not raise serious prejudice and problems about private international law.

However, Option 6 also raises certain concerns, namely the following: First, it is dubious whether a regulation can achieve full harmonisation. One can also express concern about the considerable costs which could be incurred

36 Basedow, J., "The Court of Justice and Private Law: Vacillations, General Principles and the Architecture of the European Judiciary", *European Review of Private Law* 18, 2010, 433–474.

during the migratory period brought about by the instrument. Since national legislatures have their own sets of neighbouring legislation that continue to run parallel with contract law, such as the law of tort, this could also result in a certain degree of legal friction.

Furthermore, adopting this type of instrument would end the competition between the different domestic contract laws, and market participants would also be restricted in terms of choice of law. A uniform law would also lose the sensitivity of certain domestic laws. This sensitivity is undoubtedly a result of certain local needs that each domestic system would have adapted. A uniform instrument would apply one regime in all territories. This may be undesirable since it could prove to be rather inflexible. One must not forget that once this regime has entered into force, its subsequent revision would undoubtedly be a difficult task at the EU level. This could lead to a "monster" regime which would not lend itself to the needs of the market and which would only create conflict between the Member States to the extent that it would bring about a *status quo* in European contract law, where Europe is presented with a regime which cannot be changed and amended by market requirements. This would surely lead to a deterioration of the Internal Market rather than complement it.

Regarding the legal basis, both Options 5 and 6 meet the requirements of Article 114 TFEU since they are designed to complement the functioning of the Internal Market, and their goals may not be reached at the member-state level. However, these policy options must also pass the proportionality and subsidiarity principle tests regarding Article 5 TEU. For this reason, Options 5 and 6 have found resistance to using Article 114 TFEU as the legal basis since there is no need for their intervention in light of the Proposal on consumer rights. Furthermore, there is no doubt that the Directive would not be able to reach its main goal, which is to reduce the transaction costs of transnational contracts, as it does not have the means to do so.[37]

Option 7 suggests a regulation establishing a European Civil Code. This may also be unjustified on the grounds of subsidiarity. Furthermore, since this Option suggests a comprehensive European Civil Code, it is practically unrealistic. This Option cannot provide Europe with the contract law instrument it is chasing since the competence issue limits its existence. This is because it is inevitable that certain areas will lack the Internal Market link. This comes as no surprise, but it results from Europe's lack of a common European core in fields such as property, family law, and the law of succession. Furthermore,

37 Hesselink, M., Rutgers, J., & de Booys, T., *The Legal Basis for an Optional Instrument on European Contract Law*, Centre for the Study of European Contract Law, Working Paper, 4/2007, 39.

opposition from Member States is imminent, so much so that the Commission itself recognises the lack of justification for such an Instrument.

4 Quo Vadis? – The Proposal of a Regulation on a Common European Sales Law (CESL) COM (2011) 635 Final

The Green Paper was followed by the Publication of an optional Regulation on similar grounds to Option 4, the Proposal of a Regulation on a Common European Sales law published in October 2011.[38] This optional character constitutes a central idea of the Proposal, beyond legal techniques, as it reveals the principle of contractual freedom that underlies the base of this Regulation and poses an essential dilemma, given that it is linked with a sphere of protected rights such as those of consumers.[39]

Hence, the next step after the Publication of the Green Paper was promulgating the Proposal for a Common European Sales Law. It appears that the actions at the EU level started with the desire for an approximation of the civil laws of the Member States. In the academic arena, this translated into the quest for a European civil code. The project seems to have eventually been diluted to a choice of policies limited to contract law in the Green Paper leading to the proposed CESL. The ultimate result was an instrument limited to European sales law solely applicable to cross-border transactions when specifically chosen by the parties (optional, opt-in). The final choice for a regulation setting up an optional instrument of European Sales Law seems not to have adopted lock stock and barrel any of the options presented in the Green Paper leading to the CESL proposal.

The European Commission has chosen the fourth Option, albeit limitedly concerning sales rather than contract law. Since the results of the Expert Group were published, the first Option has also been taken on in conjunction with the optional Regulation on sales law. Reference to the proposed CESL as a sales law is not exact, even though this is what its title provides for. The proposed CESL also covers services contracts, though only those: a) related to sales contracts covered by the proposed CESL; b) for services provided by the seller; and c) in the case of a separate service contract, concluded at the same time as the sales contract.

38 Proposal on a Common European Sales Law, COM (2011) 635 final.

39 Sanchez-Lorenzo, S., "Common European Sales Law and Private International Law: Some Critical Remarks", *Journal of Private International Law*, Vol. 10 No. 2, 191.

Hence, the proposed CESL, rather than regulating services contracts in general, adapts the sales contract rules to cater for related services contracts, creating a form of contract unknown to the Member States, which have laws regulating services contracts generally and not related services contracts. The proposed CESL focuses on sales law, and the related services law regime is ancillary, having been introduced in the Proposal to maximise the added value to the Common European Sales Law. So much so that persons not part of the sales contract cannot offer related services regulated by the CESL. A related service can be provided in the sales contract or a separate service contract. The proposed CESL is a cautious step because a) it was the chosen Option instead of the more encompassing options providing for an EU contract law or civil code; b) the proposed Regulation itself is limited to cross-border sales contracts only; c) it has a limited personal scope covering solely trader/consumer transactions or transactions between traders where one of the parties is an SME; d) it fails to provide comprehensive services contract law, an area which, to date, is not yet harmonised at EU level; and e) it is optional. Hence, it does not replace national laws because of its limited scope.

As discussed previously, the developments leading to the proposed CESL have been outlined. It was pointed out that the project started with plans seemingly leading to a European civil code. The plans were then limited to a contract law project and finally transformed into an optional sales law applicable to cross-border transactions. It has further been discussed that, in the context of the sensitive character of the subject matter at hand, characterising the instrument as optional and limiting it to sales law might have been a wise move by the European Commission to attract the acceptability of the instrument. The other side of the coin is that several scholars and jurists have already expressed their opinions and baptised the Proposal for a CESL as a "Trojan horse",[40] that is, an optional instrument which *prima facie* is harmless to national laws but which may well develop into full harmonisation through the backdoor—the same full harmonisation that the EU has failed to achieve in consumer law through the very recent experience of the Consumer Rights Directive (CRD).[41] The emphasis here is on the potential of the optional instrument to regulate

40 The term was used by the House of Lords' EU Committee in reports referring to the DCFR. See EU Committee, *European Contract Law: the draft Common Frame of Reference* (HL 2008–9, 12) para. 59.

41 Directive 2011/83/EU of the European Parliament and of the Council of 25 October, 2011 on consumer rights, amending Council Directive 93/13/EEC and Directive 1999/44/EC of the European Parliament and of the Council and repealing Council Directive 85/577/EEC and Directive 97/7/EC of the European Parliament and of the Council [2011] OJ L304/64 (CRD).

contracts involved in the functioning and enhancement of the Internal Market: an instrument which has the prospect of ameliorating dialogue amongst the national systems and is capable of bringing together those aspects which would otherwise not reach full harmonisation at EU level either because of a lack of consensus or because they are not within the competence of the EU.

Before the actual publication by the European Commission of the proposed CESL, Lando has been quoted expressing his desire that the next step should be that an optional instrument be prepared and that after that: "when a complete instrument is ready, the Optional Instrument should become an opt-out instrument, and in the final stage, it should become a European Civil Code of Contracts".[42] This desire, which is much welcomed by those advocating further harmonisation, sends shivers down the spine of those resisting harmonisation in this area of law. Such statements opined by one of the most adamant supporters for promulgating a European civil code inevitably strengthen the beliefs of those characterising the proposed CESL as a Trojan horse.

It can be argued that the risk of backdoor harmonisation only arises if the optional instrument is chosen in the parties' dealings. Should the optional instrument be unpopular and hence not used, it will not remove trade obstacles and even less assist in the convergence of EU and national laws in the context of contract law. Some scholars have opined that the proposed CESL is a one-armed juggler, lacking the essential elements and impinging on fundamental matters that will result in its non-use.[43] The claims include the lack of respect for the philosophy of the Rome I Regulation, reference to the potential infringement of the Member States' *ordre public*,[44] social dumping,[45] a lack of predictability, and a lack of consideration for the spirit behind the rejection of maximum harmonisation through the CRD.[46] The conclusion to this discussion is simple but pragmatically presents two possible but opposing views: the proposed CESL (if eventually approved) will either harmonise sales law without appearing to do so, or it will not be used and will fail. For completeness, as explained at the end of this sub-section, the Commission withdrew the Proposal in December 2014 as it lacked support in the Council.

One can also examine the relationship between the Rome I Regulation, discussed in Chapter 4 and the choice by the European Commission of a regulation

42 Cravetto, C., "Conference Report: Towards a European Contract Law" 2011, *ERCL* 19: 1031.

43 Cartwright, J., "Choice is Good, Really?" 12. http://ec.europa.eu/justice/news/consulting_public/0052/contributions/52_en.pdf accessed 15 December 2023, contribution to COM (2010) 348 (n. 35).

44 Kuipers, J., "The Legal Basis for a European Optional Instrument, European Review of Private Law" 2011, *ERCL* 19: 545.

45 Rutgers, J., "An Optional Instrument and Social Dumping Revisited" 2011, *ERCL* 7: 350.

46 Rutgers, J., "An Optional Instrument and Social Dumping" 2006, *ERCL* 6: 199.

setting up an optional European Sales law, which law, on its enactment, shall be part and parcel of the laws of the Member States. The explanatory memorandum to the proposed CESL provides that the proposed Regulation is:[47]

> A self-standing uniform set of contract law, including provisions to protect consumers, the Common European Sales Law, which is to be considered as a *second contract law regime* within the national law of each Member State.

The European Commission unequivocally states that the new law shall become part of the Member States' national laws, but it shall not change or replace existing laws. The CESL will run parallel to the existing national laws. It is apt to point out that the choice of words by the European Commission here seems to be not accidental—the European Commission specifically refers to a second regime of laws rather than a 29th regime. The distinction is subtle but pragmatic in that a 29th regime may be considered an additional legal regime to the existing twenty-eight from which the parties to a contract can choose (hence a matter of private international law). On the other hand, reference to a second regime still provides the parties with a choice between two domestic laws, that of the particular Member State and the optional CESL (hence a matter of private law).

A choice in favour of the second regime prevents the application of the overriding mandatory provisions present in the existing national laws of the particular Member States as required by Rome I. Admittedly, this is a step ahead in that other optional regime, such as the Vienna Convention are limited by the application of mandatory rules. In this context, Vanessa Mak argues that the second regime provides "an easy route for the European Commission to proceed with the 'optional instrument' project without facing the (unwanted) problem of changing the Rome-I Regulation".[48] Reisenhuber looks at the matter from a regulatory competition point of view and opines the following when discussing the CFR:[49]

> The bottom line is: the Union has a double function. With the Rome I-Regulation, it sets important rules for the regulatory competition in contract law. And with the CFR, it enters competition with its own 'product'. Now it is deliberately designing the rules so as to favour its own product—' You can't beat the house'.

47 COM (2011) 635 final.

48 Mak, V., "Policy Choices in European Consumer Law" 2011, *ERCL*, 7: 271.

49 Riesenhuber, K., "A Competitive Approach to EU Contract Law" 2011, *ERCL*, 7: 130–131.

The other side of the coin is that in cross-border business-to-consumer (B2C) contracts, the consumer is devoid of the protection of the mandatory rules of his/her country. Hence, the consumer might be losing out unless the level of consumer protection of the optional instrument is such as providing protection equal to or more than that provided by the law of the Member State of the consumer. In cross-border business-to-business (B2B) contracts, the inapplicability of the Rome I Regulation boils down to the inapplicability of the mandatory provisions, usually deemed to constitute the *ordre public* of the jurisdiction and part and parcel of the country's legal core.

In this context, the proposed CESL is converging the mandatory rules of Member States. To add to the complexity of the matter, Kuipers opines that convergence in this sense would "boil down to a harmonisation of public policy".[50] If this is the case, the probability is that, for the proposed CESL to be an acceptable text for all the twenty-eight Member States, all interests covered by all mandatory provisions in all the twenty-seven Member States must be catered for in the CESL—this simply cannot be the case, because of practical impossibility. The Green Paper and explanatory memorandum to the proposed CESL seem to offset this deficiency by referencing the benefits that businesses and consumers alike should experience due to a more developed single market the proposed CESL should provide for. Hence, presumably, the market rationale here overrides the *ordre public* of Member States.

The above opens the gates for regulatory arbitrage. Businesses transacting cross-border might choose to apply the applicable law and not the optional instrument or vice versa depending on the applicable mandatory laws and on which legal regime mostly benefits them. In such cases, the consumer does not make a free choice but clicks—"I accept" for the terms and conditions of the law that businesses/traders decide to offer. On another note, the proposed CESL allows Member States to apply the CESL to domestic (as opposed to cross-border) transactions. In this context, the applicability of the Rome I Regulation is excluded as it is not a matter of private international law. Hence, the Member States' mandatory provisions are unaffected. In such cases, the domestic conflict of law rules would apply in case of conflict between the CESL and overriding mandatory rules. Presumably, a national court of law would favour applying mandatory laws instead of any other domestic law.

On 16 December 2014, the EU Commission presented its Work Programme 2015 to the European Parliament. The general theme was a thinning down of initiatives and concentration on those most likely to succeed and to have a

50 Kuipers, J., "The Legal Basis for a European Optional instrument" 2011, *ERCL* 19: 45.

positive impact. Given all the work done and the positive and liberating effect it could have for SMEs trying to trade online across Europe, the existing Proposal for a CESL is listed as item 60 in the Annex of withdrawn proposals.[51] However, the reason given for the withdrawal is "Modified proposal to fully unleash the potential of e-commerce in the Digital Single Market". This new emphasis was stressed in the speech by the First Vice-President Frans Timmermans, who said that one of the Commission's priorities for 2015 would be an ambitious digital single market package which would, among other things, modernise copyright laws and simplify rules for consumers making online digital purchases.[52]

It remains to be seen what the modified Proposal will look like. Presumably, it will consider amendments proposed by the European Parliament in a new and well-integrated way. The opportunity will be there to make other changes. For example, if it is designed to make online consumer purchases easier, the rules on opting into the instrument should be much simpler. The name should also be reconsidered. The name "Common European Sales Law" invites the misconception that this is a law which would replace national sales laws. This misconception is used by opponents of most EU initiatives who can say that they consider existing national laws to be good enough. The name of the new instrument should reflect that it would (if this is indeed the case) be an optional instrument that would not[53] replace existing national laws.

5 Conclusion

Almost another decade has passed since then. No more substantive proposals were made, and the European Projects remain an academic exercise. Despite this, the idea of such a code should not be rejected altogether, but it has to be recognised that a European Civil Code will not be the same kind of beast as traditional national civil codes.[54] Such a code has to be constructed within a multi-level system of governance.[55] It will share some features of traditional

51 http://www.epln.law.ed.ac.uk/2015/01/07/proposal-for-a-common-european-sales-law-withdrawn/ last accessed on 15 December 2023.

52 http://www.epln.law.ed.ac.uk/2015/01/07/proposal-for-a-common-european-sales-law-withdrawn/ last accessed on 15 December 2023.

53 http://www.epln.law.ed.ac.uk/2015/01/07/proposal-for-a-common-european-sales-law-withdrawn/ last accessed on 15 December 2023.

54 Mattei, U., *The European Codification Process—Cut and Paste,* Kluwer, 2003, 121 *et seq.*

55 Joerges, C., "European Challenges to Private Law: On False Dichotomies, True Conflicts and the Need for a New Constitutional Perspective" 1998, *Legal Studies* 18(2): 146.

codes, but significant differences must be acknowledged. It will probably resemble national codes in its systematic articulation of principles governing fair dealings and respect for the interest of others concerning civil society. However, as a practical instrument of government, it must differ from national codes. In particular, in the absence of a federal court system, it will not be possible to ensure the consistent interpretation, application and enforcement of a European Civil Code. Traditional civil codes invariably promise more than they can deliver, and there is usually an inevitable tension between the twin ambitions of transparency and systematic legal reasoning. Any European Civil Code proposal will likely face the same criticisms. Such a code based on the existing models of civil codes in nation-states might equally be proved incapable of adaptation to obstruct innovation and prevent coherence. Critics of codes are unlikely to favour the common law system instead, as this is probably regarded as equally defective in these respects.[56] However, these arguments may be rejected for such a project as a European Civil Code, which consists of an attempt to articulate a coherent set of principles to govern civil society and is not required to make European law more effective or adaptable. The short-term future will likely be more fragmentation (chaos), more harmonisation and less consolidation or codification.

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PART 2

Digital Rights

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CHAPTER 5

Regulating Automated Decision-Making in the European Union: Article 22 GDPR and the Internal Market

Mireille M. Caruana

Abstract

In this chapter, the author will critically analyse Article 22 GDPR in light of its role as a provision intimately connected with the Internal Market and pursuing the common goal of achieving a fair and balanced digital economy that respects the rights and interests of individuals, businesses and governments. In doing so, it will engage in a critical analysis of the SCHUFA judgement (case C-634/21), the recent and first direct ruling by the CJEU on Article 22, focusing on those elements that the judgement has helped clarify and those that remain subject to considerable interpretative uncertainty, such as the right of an ex-post explanation of automated decisions.

1 Introduction[1]

The General Data Protection Regulation (GDPR) regulates certain instances of 'automated individual decision-making, including profiling'. 'Automated decision-making' refers to making a decision solely by automated means without any human involvement. In contrast, 'profiling' refers to the automated processing of personal data to evaluate an individual's personal aspects, 'such as automatic refusal of an online credit application or e-recruiting practices without human intervention.[2]

The Internal Market relies on the free movement of personal data between Member States, which is essential for economic and social integration and the development of the digital economy. Therefore, the GDPR furthers the harmonisation of rules regarding the protection of personal data in order to ensure the free flow of such data within the Internal Market. In its regulation

1 This chapter states the position as at 30th April 2024. At time of writing, the AI Act has received the approval of the European Parliament, but is still not formally enacted.

2 Recital (71) GDPR.

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of automated decision-making processes, the European Union aims to balance the rights of individuals and the interests of the business and government sectors, all within the ambit of the digital economy.

Article 22 of the GDPR allows automated decision-making, including profiling, only in certain circumstances, provided suitable safeguarding measures are implemented. At the same time, Article 22 of the GDPR implicitly recognises the benefits of automated decision-making for innovation, efficiency, and competitiveness in the Internal Market.

This chapter first introduces the problematics of automated decision-making and the rationale of Article 22 of the GDPR. It proceeds to an overview of the relevant articles of the GDPR regulating systems using personal data for 'automated decision-making, including profiling'. It critically analyses Article 22 of the GDPR in light of its role as a provision intimately connected with the Internal Market and pursuing the common goal of achieving a fair and balanced digital economy that respects the rights and interests of individuals, businesses and governments. Recently, the CJEU delivered its first direct ruling on Article 22,[3] clarifying some aspects, though interpretative ambiguities persist. Finally, it considers alternative provisions of the GDPR, specifically on data protection impact assessments and data protection by design, that may provide a more effective means of protection against algorithmic harms by adopting a paradigm which seeks to avert harm by ensuring the fairness and non-discriminatory nature of deployed systems.

2 Problematics of Artificial Intelligence

In February 2021, the Dutch Prime Minister and his entire cabinet resigned following a scandal concerning the use by the Dutch tax authorities of an automated decision-making algorithm to detect instances of tax fraud that resulted in thousands of families being wrongly accused of social benefits fraud 'partially due to a discriminatory algorithm' and consequently cut off from benefit payments.[4] An investigation from the Dutch Data Protection Authority found

3 Case C-634/21 *SCHUFA Holding* (*Scoring*) [2024] ECLI:EU:C:2023:957.

4 Melissa Heikkilä, *Dutch scandal serves as a warning for Europe over risks of using algorithms* (POLITICO 2022) <https://www.politico.eu/article/dutch-scandal-serves-as-a-warning-for-europe-over-risks-of-using-algorithms/> accessed 20 March 2023; Amnesty International Report: Xenophobic Machines: Discrimination through Unregulated use of Algorithms in the Dutch Childcare Benefits Scandal (Amnesty International 2021) <https://www.amnesty.org/en/documents/eur35/4686/2021/en/> accessed 20 March 2023.

that the algorithms deployed were discriminatory because they took variables such as whether someone had a second nationality into account.[5]

Other reports concerned the development of predictive policing technology[6] that perpetuated racial/ethnic profiling as a result of a model trained on biased and prejudiced data.[7] Amnesty International has produced a report on a pilot project called 'the Sensing Project' in the city of Roermond, dubbing the project "the automation of ethnic profiling'" and calling it "discriminatory by design".[8]

Similar reports have emerged concerning deploying AI systems in the private sector. For example, Amazon.com Inc's AMZN.O developed an algorithm that used Artificial Intelligence to review job applicants' resumès. The company realised that the system was not rating candidates for software development and other technical jobs in a gender-neutral way because the computer models were trained with data from resumès submitted to the company over ten years, most of which came from men – a reflection of male dominance across the tech industry. The model detected this pattern and replicated it.[9]

Thus, rather than overcome human bias, an AI system may merely replicate it. Worse still, in the words of the UN Special Rapporteur on contemporary forms of racism, racial discrimination, xenophobia and related intolerance:

> The public perception of technology tends to be that it is inherently neutral and objective, and some have pointed out that this presumption of technological objectivity and neutrality is one that remains salient even among producers of technology. But technology is never neutral – it

5 Reported in Dutch here <https://www.volkskrant.nl/nieuws-achtergrond/belastingdienst-schuldig-aan-structurele-discriminatie-van-mensen-die-toeslagen-ontvingen~baebefdb/?referrer=https%3A%2F%2Fwww.vice.com%2F>.

6 Defined by Amnesty International as 'The application of analytical techniques across large datasets in an attempt to enable early identification of potential crime problems'. Amnesty International, *We Sense Trouble: Automated Discrimination and Mass Surveillance in Predictive Policing in the Netherlands* (2020) <https://www.amnesty.org/en/documents/eur35/2971/2020/en/> accessed 20 March 2023.

7 Gabriel Geiger, The Netherlands Is Becoming a Predictive Policing Hot Spot (Vice 2020) <https://www.vice.com/en/article/5dpmdd/the-netherlands-is-becoming-a-predictive-policing-hot-spot> accessed 20 March 2023.

8 Amnesty International, *We Sense Trouble: Automated Discrimination and Mass Surveillance in Predictive Policing in the Netherlands* (2020) <https://www.amnesty.org/en/documents/eur35/2971/2020/en/> accessed 20 March 2023.

9 Jeffrey Dastin, Amazon Scraps Secret AI Recruiting Tool That Showed Bias Against Women (Reuters 2018) https://www.reuters.com/article/us-amazon-com-jobs-automation-insight-idUSKCN1MK08G.

reflects the values and interests of those who influence its design and use, and is fundamentally shaped by the same structures of inequality that operate in society.[10]

3 Rationale for Article 22 GDPR

Article 22 of the GDPR addresses the risks that may flow from automated or algorithmic decision-making. The provision closely reflects a corresponding article from the Data Protection Directive (DPD),[11] which preceded the GDPR. Animating Article 15 DPD was a "fear for the future of human dignity in the face of machine determinism".[12] This means humans should maintain ultimate control and responsibility for decisional processes that significantly affect other humans. This is brought forward in recital (4) of the GDPR, which states, "The processing of personal data should be designed to serve mankind". The foundations of the GDPR are thus embedded in fundamental human rights, essential to upholding human dignity and democratic structures.

The concern of the GDPR goes beyond issues of privacy, data protection and confidentiality to encompass other concerns relating to a broader spectrum of human rights, particularly the fundamental right of non-discrimination.[13] This is reflected in the recital (71) of the GDPR, which mentions "factors which result in inaccuracies in personal data" and the "risk of errors", as well as "the potential risks involved for the interests and rights of the data subject, (…) *inter alia*, discriminatory effects on natural persons" based on the "special categories" of personal data as defined in the GDPR and which include, for example, racial or ethnic origin, religion, genetic or health status, and sexual orientation.

10 Tendayi Achiume, *Racial discrimination and emerging digital technologies: a human rights analysis* – Report of the Special Rapporteur on contemporary forms of racism, racial discrimination, xenophobia and related intolerance (Human Rights Council, Forty-fourth session, 15 June – 3 July 2020) A/HRC/44/57 <https://documents-dds-ny.un.org/doc/UNDOC/GEN/G20/151/06/PDF/G2015106.pdf?OpenElement> accessed 20 March 2023.

11 Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data, OJ L 281/31.

12 Lee A. Bygrave, 'Minding the Machine v2.0: The EU General Data Protection Regulation and Automated Decision Making' in Karen Yeung and Martin Lodge (eds.), *Algorithmic Regulation* (Oxford University Press 2019), 249.

13 Article 21 Charter of Fundamental Rights of the European Union C 326/391.

The purpose of regulating automated decision-making is to address the risks that such algorithmic decision-making processes pose. Thinking creatively regarding safeguards, accountability, effective remedies, and redress is necessary. AI-powered 'black box' systems consisting of self-learning algorithms devoid of human oversight and supervision result in a lack of transparency, thus diminishing human control over, and responsibility for, decisional processes. Nevertheless, addressing the lack of transparency alone is not sufficient, and transparency may not be "the remedy you are looking for".[14] For example, in the context of historical data returned by the Google search engine, rather than an explanation of the decisional process, the effective remedy consisted of de-referencing by the search engine.[15]

Unfairness and discrimination through algorithms are a growing concern because of the increasing use of these systems in various sectors, coupled with the lack of regulation and transparency around their development and use. Accordingly, it is important to ensure algorithms are designed and used fairly and transparently to avoid perpetuating bias and discrimination. This may involve providing more transparency into how algorithms make decisions.

4 Article 22: Overview

In overview, Article 22 provides that:

i. the data subject has "the right not to be subject to a decision based solely on automated processing, including profiling", which produces legal or similarly significant effects;
ii. there are exceptions to this rule;
iii. where those exceptions apply, suitable measures to safeguard the data subject's rights and freedoms and legitimate interests must be in place;
iv. decisions based on those exceptions must not be based on special categories of personal data listed in Article 9, unless the data subject has given explicit consent or there is a substantial public interest involved and suitable measures to safeguard the data subject's rights and freedoms and legitimate interests are in place.

14 Lilian Edwards and Michael Veale, 'Slave to the Algorithm? Why a 'Right to an Explanation' Is Probably Not the Remedy You Are Looking For' (2017) 16 Duke Law & Technology Review 18.

15 Case C 131/12 *Google Spain SL and Google Inc. v Agencia Española de Protección de Datos (AEPD) and Mario Costeja González* ECLI:EU:C:2014:317.

5 Scope

The right in Article 22(1) applies when (1) a 'decision' is made which is (2) based solely on automated processing, including profiling and (3) produces legal effects or similarly significantly affects the data subject.

The right is operationalized by reference to 'the data subject'. In AI models, the data used to train the AI system may not include any data relating to the subject affected by the decision. Thus, the decision need not be based on data relating to that person. As the Article 29 Working Party (A29WP)[16] observes, automated decisions can be based on any data, for example:

- data provided directly by the individuals concerned (such as responses to a questionnaire);
- data observed about the individuals (such as location data collected via an application);
- derived or inferred data such as a profile of the individual that has already been created (e.g. a credit score).[17]

Nevertheless, the decision will ultimately involve data processing on that person.

5.1 *'A Decision'*

Recital 71 GDPR expounds that the data subject should have the right not to be subject to "a decision, which may include a measure (…)". A decision is the outcome of an automated processing system, while a measure is an action taken as a result of that decision. A decision can produce one or more measures, depending on the circumstances involved. A decision could be about exercising government agency authority or a private commercial entity. The term decision should be interpreted in a fairly generic sense.[18]

In the first case brought before the CJEU requiring the Court to rule directly on Article 22, a credit information service providing its customers (financial institutions) with creditworthiness assessments consisting of "the automated establishment of a probability value concerning the ability of the data subject to honour a loan in the future" without further recommendation or comment,

16 The Article 29 Working Party (A29WP), superseded by the European Data Protection Board (EDPB), issues general guidance (including guidelines, recommendations and best practice) to clarify the law and to promote common understanding of EU data protection laws. Such guidelines do not however have the force of law.

17 A29WP 2018 Guidelines, p. 8.

18 Isak Mendoza and Lee A. Bygrave 'The Right not to be Subject to Automated Decisions based on Profiling', in Synodinou, Jougleux, Markou and Prastitou (eds.), *EU Internet Law: Regulation and Enforcement* (Springer 2017) 87.

claimed that it only provides information to its customers, who in turn take the actual decisions concerning credit agreements. As defined by the AG, the matter concerned "whether the decision-making procedure is designed in such a way that the scoring carried out by the commercial information company predetermines the decision of the financial institution to grant or refuse credit".[19] If in its decision-making procedure the financial institution gives paramount importance to the scoring transmitted by the credit information service, and since a negative score can, on its own, produce unfavourable effects for the person concerned, qualifying it as a 'decision' seems justified. In this instance, the facts of the case indicate that the scores established by the credit information service and communicated to the financial institution play a decisive or determining role when granting loans and designing their conditions.[20] It follows that the score itself must be considered as having the quality of a 'decision' within the meaning of Article 22(1) GDPR.[21] The AG opined that this is essentially a question of fact which can best be assessed by the national courts in each particular case, as the answer to this question depends on internal rules and practices of the financial institution in question, which must generally leave it no leeway as to the application of the score to a credit application.[22]

5.2 *'Based Solely on Automated Processing, Including Profiling'*

Article 22(1) applies only to decisions based 'solely' on automated processing. While the initial data capture may not be fully automated but could be manual or semi-automated, Article 22 would still be engaged, provided the data upon which the decision is based are digital.

A decision is not considered to be based 'solely' on automated processing if there is human involvement. The A29WP considers that to qualify as human involvement, "the controller must ensure that any oversight of the decision is meaningful, rather than just a token gesture. Someone should do it with the authority and competence to change the decision".[23] Thus, a decisional support tool falls clear of Article 22.

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19 C-634/21 *Shufa Holding* (*Scoring*) [2023] ECLI:EU:C:2023:220, Opinion of AG Pikamae, para 42. Note: The Advocate General's Opinion is not binding on the Court of Justice. It is the role of the Advocates General to propose to the Court, in complete independence, a legal solution to the cases for which they are responsible.

20 C-634/21 *Shufa*, Opinion (n 19) para 43, paras 46–52.

21 C-634/21 *Shufa*, Opinion (n 19) para 47.

22 C-634/21 *Shufa*, Opinion (n 19) para 44.

23 A29WP 2018 Guidelines, 21.

This matter was at issue in the *SCHUFA Holding* (*Scoring*) case. While from the facts of the case, it appeared that the creditworthiness assessment conducted by SCHUFA is indeed fully automated, the financial institution to which SCHUFA communicates the score is called upon to adopt an ostensibly autonomous act with regard to the person concerned, namely the granting or refusal of credit. Therefore, should SCHUFA's profiling procedure (and subsequent assessment) be viewed as a decisional support tool for credit granting (or refusal), Article 22 would not be engaged. Referring to the facts of the case[24] and making an argument for effective protection,[25] the Advocate General concluded that a "decision based solely on automated processing' is indeed taken by SCHUFA, as 'in accordance with consistent practice" the financial institution "bases its decision relating to the establishment, the execution or termination of a contractual relationship with this same person in a decisive manner on said value".[26]

In a case concerning Uber drivers who challenged the deactivation of their accounts and consequent termination of their contracts due to alleged fraudulent actions, the Amsterdam District Court concluded that there were no fully automated decisions. The applicants did not contest Uber's explanations about their decision-making process, and thus, they were accepted by the court. Uber stated that the relevant decisions were made by (at least) two employees of the risk team based on an investigation conducted by an employee in response to fraud signals. One of those decisions was even made after an Uber employee investigated the signals about using the manipulated app and spoke to the driver. The Court ruled that this involved significant human intervention.[27] The Court consequently denied the drivers access to meaningful information concerning the algorithm according to Article 15 of the GDPR.[28]

The scope of the provision embraces decisions based solely on automated processing that may, but need not, involve profiling. Article 4(4) GDPR defines 'profiling' as "any form of automated processing of personal data consisting of the use of personal data to evaluate certain personal aspects relating to a natural person, in particular, to analyse or predict aspects concerning that natural

24 C-634/21 *Shufa*, Opinion (n 19) para 46.

25 C-634/21 *Shufa*, Opinion (n 19) paras 48–51.

26 C-634/21 *Shufa*, Opinion (n 19) para 59.

27 Uber deactivation judgement, para 4.24. Unofficial English translations available: <https://ekker.legal/en/2021/03/13/dutch-Court-rules-on-data-transparency-for-uber-and-ola-drivers/> accessed 21 March 2023.

28 Uber deactivation judgement, para 4.26. For commentary see: Raphaël Gellert, Marvin van Bekkum, and Frederik Zuiderveen Borgesius, 'The Ola & Uber judgments: for the first time a court recognises a GDPR right to an explanation for algorithmic decision-making' (EU Law Analysis, 28 April 2021) <http://eulawanalysis.blogspot.com/2021/04/the-ola-uber-judgments-for-first-time.html> accessed 21 March 2023.

person's performance at work, economic situation, health, personal preferences, interests, reliability, behaviour, location or movements". In the SCHUFA (Scoring) case, Advocate General Pikamäe opined that the automated establishment of a credit score, which reflects a probability concerning an individual's likelihood to repay a loan in the future, constitutes profiling under the GDPR.[29] The CJEU confirmed this.[30] In practice, many, if not most, types of automated decision-making will include profiling.[31]

5.3 *Producing 'Legal Effects' or 'Similarly Significant Effects' for the Interested Party*

Applying Article 22(1) requires that the decision has serious consequences for the data subject insofar as it produces "legal" or "similarly significant" effects. A legal effect requires that the decision affects the data subject's legal rights, legal status or rights under a contract. Examples of 'legal effects' include automated decisions about an individual that result in:

- the establishment, execution or termination of a contractual relationship;
- entitlement to or denial of a particular social benefit granted by law, such as a child or housing benefit;
- refused admission to a country or denial of citizenship.[32]

Using the word 'similarly' in 'similarly significant effects' ties the notion of 'significant effects' to 'legal effects'. Therefore, only the effects that have a serious impact will be covered by this provision.[33] In the Opinion of the Article 29 Working Party (A29WP), subsequently endorsed by the European Data Protection Board (EDPB), a 'significant' effect is produced when a decision has the potential to

- significantly affect the circumstances, behaviour or choices of the individuals concerned;
- have a prolonged or permanent impact on the data subject or
- at its most extreme, lead to the exclusion or discrimination of individuals.[34]

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29 C-634/21 *Shufa*, Opinion (n 19) para 33.

30 Case C-634/21 *SCHUFA Holding* (*Scoring*) [2024] ECLI:EU:C:2023:957, para 47.

31 Maja Brkan, 'Do Algorithms Rule the World? Algorithmic Decision Making and Data Protection in the Framework of the GDPR and Beyond' (2019) 27(2) International Journal of Law and Information Technology 91, 97.

32 Article 29 Data Protection Working Party, Guidelines on Automated individual decision-making and Profiling for the purposes of Regulation 2016/679 Adopted on 3 October 2017 As last Revised and Adopted on 6 February 2018. WP251rev.01, 21.

33 C-634/21 *Shufa*, Opinion (n 19) para 34.

34 EDPB, Endorsement 1/2018 (25 May 2018) (endorsing Article 29 Data Protection Working Party, Guidelines on Automated individual decision-making and Profiling for the purposes of Regulation 2016/679 Adopted on 3 October 2017 As last Revised and Adopted on 6 February 2018. WP251rev.01), 21.

The EDPB opines that the following decisions could fall into this category:
- decisions that affect someone's financial circumstances, such as their eligibility for credit;
- decisions that affect someone's access to health services;
- decisions that deny someone an employment opportunity or put them at a serious disadvantage;
- decisions that affect someone's access to education, such as university admissions.[35]

The SCHUFA case concerned precisely a decision that affected someone's financial circumstances. Indeed, AG Pikamäe noted that the decision made by the credit information service provider produces both 'legal' and 'economic' effects. Insofar as it constitutes a step prior to the conclusion of a loan contract, the economic consequences are such that they produce effects that are similarly significant as the legal effects.[36]

Another concrete instance of a situation where a court found a "legal or similarly significant effect" to be produced by an automated decision-making system was the system employed by Ola, a ridesharing company, that resulted in the imposition of penalties and deductions.[37] The Amsterdam District Court ruled that the decision to impose a discount or fine has "effects that are important enough to merit attention and that significantly affect the behaviour or choices of the person concerned as referred to in the Guidelines".[38] The automated decision led to a sanction that affected the data subject's rights under the agreement with Ola. However, with regard to the driver's 'earning profile' aspect of the same automated system that resulted in decisions to award (or withhold) a bonus, the same Court ruled that "Although the possibility of obtaining a bonus will have some influence on the driver's behaviour, it has not been shown to have legal or significant effects as referred to in the Guidelines".[39] The latter conclusion was also reached with regard to the 'Guardian'

35 EDPB, Endorsement 1/2018 (25 May 2018) (endorsing Article 29 Data Protection Working Party, Guidelines on Automated individual decision-making and Profiling for the purposes of Regulation 2016/679 Adopted on 3 October 2017 As last Revised and Adopted on 6 February 2018. WP251rev.01), 22.

36 C-634/21 *Shufa*, Opinion (n 19) para 35.

37 Amsterdam District Court, 11 March 2021, C / 13/689705 / HA RK 20-258, para 4.51.

38 *Ibid*. [unofficial English translations available <https://ekker.legal/en/2021/03/13/dutch-Court-rules-on-data-transparency-for-uber-and-ola-drivers/>].

39 Amsterdam District Court, 11 March 2021, C / 13/689705 / HA RK 20-258, para 4.47 [unofficial English translations available <https://ekker.legal/en/2021/03/13/dutch-Court-rules-on-data-transparency-for-uber-and-ola-drivers/>].

system to detect irregularities, used to monitor journeys to promote driver and passenger safety,[40] and the system for assigning trips.[41]

In the *Uber* (employment) judgement, the same Amsterdam District Court examined the algorithm-mediated matching of drivers and passengers to allocate available rides. In the Court's view, the drivers did not adequately motivate why there was a 'legal' or 'significant effect' as per Article 22 GDPR.[42]

The linkage of legal and 'similarly' significant effects leads to doubts concerning whether behaviourally targeted advertising will ordinarily meet the significant effects threshold. The decision to present targeted advertising based on profiling will not usually have a 'legal or similarly significant effect' on individuals. However, depending on the particular characteristics, it may potentially have such 'similarly significant' effects. The A29WP/EDPB highlight the following characteristics:

– the intrusiveness of the profiling process, including the tracking of individuals across different websites, devices and services;
– the expectations and wishes of the individuals concerned;
– the way the advert is delivered or
– using knowledge of the vulnerabilities of the data subjects targeted.[43]

Such targeted advertising might, therefore, meet the 'similarly significant' threshold if 'it involved blatantly unfair discrimination with non-trivial economic consequences'.[44]

Moreover, the 'significant effects' contemplated in the legal provision are measured in relation to the individual data subject concerned rather than by reference to the 'average' person. In the context of a discussion on whether targeted advertising may, in principle or a particular instance, have a 'similarly significant effect' on a data subject, Brkan opines that Article 22 GDPR requires that "the decision significantly affects a particular data subject ('him or her') and not an average one".[45] Considering the 'average' rather than the actual consumer targeted with the advertising "might not take into account particular

40 Amsterdam District Court, 11 March 2021, C / 13/689705 / HA RK 20-258, para 4.48–4.49.
41 Amsterdam District Court, 11 March 2021, C / 13/689705 / HA RK 20-258, para 4.50.
42 Amsterdam District Court, 11 March 2021, C / 13/687315 / HA RK 20-207, para 4.66–4.67.
43 A29WP 2018 22.
44 Lee A. Bygrave 'Article 22. Automated individual decision-making including profiling' in *The EU General Data Protection Regulation* (*GDPR*) *A Commentary* (OUP 2020) 534–5.
45 Maja Brkan, 'Do Algorithms Rule the World? Algorithmic Decision Making and Data Protection in the Framework of the GDPR and Beyond' (2019) 27(2) International Journal of Law and Information Technology 91, 103.

vulnerabilities of a data subject, such as sicknesses, addictions, anxieties or traumatic past experiences".[46]

Individual harm can also result from group harm because of the attributes of a particular group to which the individual belongs and which is relevant to the decision made. An automated decision may have 'significant effects' on individuals as members of a group, for example, if a person's creditworthiness is determined not by her or his individual credit history but rather by his geophysical address.

When the affected/harmed group consists of a vulnerable group, such as children, this lowers the threshold of 'similarly significant effects'. Recital (38) GDPR posits that "children merit specific protection with regard to their personal data" and that such protection should "in particular, apply to the use of personal data of children for the purposes of marketing or creating personality or user profiles". Furthermore, recital (71) expands that a measure evaluating personal aspects based solely on automated processing and which produces legal or similarly significant effects "should not concern a child".

6 Right or Prohibition?

An ongoing controversy in the literature concerns whether the enigmatic 'right not to be subject' to an automated decision is to be interpreted as a general, qualified prohibition or rather as a *right* to be exercised at the data subject's discretion. The A29WP has interpreted Article 22(1) as establishing a *general prohibition* on fully automated individual decision-making, including profiling with a legal or similarly significant effect.[47]

However, academic opinion on this matter is divided. It has been convincingly argued that "such a provision is better characterized as conferring upon data subjects a right that they may exercise at their discretion, rather than establishing a general ban on individual decisions based solely on automated processing".[48] This interpretation is strongly supported by the fact that other provisions of the GDPR assume the existence of this type of processing; for example, the transparency duties, which require the communication

46 *Ibid.*

47 A29WP 2018, p.19. "Interpreting Article 22 as a prohibition rather than a right to be invoked means that individuals are automatically protected from the potential effects this type of processing may have". A29WP 2018, 20.

48 Luca Tosoni. The right to object to automated individual decisions: resolving the ambiguity of Article 22(1) of the General Data Protection Regulation. *International Data Privacy Law*, 2021, Vol. 11, No. 2.

of information to the data subject regarding "the existence of automated decision-making, including profiling, referred to in Article 22(1) and (4)". Furthermore, this interpretation is consistent with the widespread deployment of such systems in both the public and private sectors where digitalization is advanced and where there may be socially justifiable benefits.[49]

Despite the convincing nature of the latter view (indeed, Bygrave opines that *lex lata* "the better view" is that Article 22(1) provides a right to be exercised at the discretion of data subjects[50]), the AG advised the Court to take a different direction and opt for a reading of Article 22(1) as a "general prohibition" of automated decision-making producing legal effects concerning or significantly affecting the data subject similarly. While acknowledging that Article 22(1) GDPR is 'special' compared to the other restrictions on the processing of data contained in the GDPR, in that it enshrines a 'right' of the data subject not to be subject to a decision based solely on automated processing, the AG opined that, notwithstanding the terminology used, the application of Article 22(1) GDPR does not require the data subject to actively invoke the right. Rather, considering the scheme of that provision, in particular paragraph 2, which sets out the cases in which such automated processing is exceptionally authorized, the provision allows the conclusion that the said provision establishes a general prohibition of decisions of the type described above.[51] The CJEU has concurred that Article 22 'lays down a prohibition in principle, the infringement of which does not need to be invoked individually by such a person'.[52]

7 Exceptions to Article 22(1)

Article 22(2) provides exceptions from Article 22(1). The latter does not apply if the decision: (a) is necessary for entering into, or performance of, a contract between the data subject and a data controller; (b) is authorised by Union or Member State law to which the controller is subject and which also lays down suitable measures to safeguard the data subject's rights and freedoms and legitimate interests; or (c) is based on the data subject's explicit consent.

49 Bygrave, 'Minding the Machine v2.0' (n 12) 253.

50 Lee A. Bygrave, 'Machine Learning, Cognitive Sovereignty and Data Protection Rights with Respect to Automated Decisions' in Ienca et al. (eds.), Cambridge Handbook of Information Technology, Life Sciences and Human Rights. Cambridge University Press 2022.

51 C-634/21 *Shufa*, Opinion (n 19) para 31.

52 SCHUFA Holding (n 3) para 52.

Where the individual has consented to such decisions, or if such decisions are necessary for entering into, or performing, a contract between the individual and the company, the data controller must 'implement suitable measures to safeguard the data subject's rights and freedoms and legitimate interests, at least the right to obtain human intervention on the part of the controller, to express his or her point of view and to contest the decision'.[53]

7.1 *Contracts*

The contractual derogation under Article 22(2) includes a 'necessity' criterion that "signals at least that the decision must have been *required* for entering into or fulfilling the contract with the data subject".[54] Mendoza and Bygrave comment, "The rationale behind the criterion is presumably to make it difficult for the data controller to escape Article 22(1) by merely pointing to a standardised contract with the data subject".[55]

A key operational issue remains regarding the precise meaning of the 'necessity' criterion in the provisions of the GDPR. Notably, 'necessary' is not as stringent and restricting as 'indispensable'. In *Huber*,[56] the CJEU assessed whether a centralized database was necessary in terms of *effectiveness*:

> … the centralisation of those data **could be necessary**, within the meaning of Article 7(e) of Directive 95/46, if it contributes to the more **effective** application of that legislation as regards the right of residence of Union citizens who wish to reside in a Member State of which they are not nationals.

Although this judgment interprets Article 7(e) Directive 95/46, the terminology of 'necessity' is used in both the GDPR and the Directive that preceded it; accordingly, the same interpretation should be applied if a new case requires a similar or equivalent assessment.

7.2 *Statutory Authority*

National legislation will likely play a major part in determining the level of protection under Article 22. Any such national legislation must provide "suitable measures to safeguard the data subject's rights and freedoms and legitimate interests". The A29WP assumes that the safeguards that will be provided for

53 Article 22(3) GDPR.
54 Bygrave, *A Commentary* (n 44) 536.
55 Mendoza and Bygrave (n 18) 92.
56 C-524/06 Huber ECLI:EU:C:2008:724.

under statutory authority will be of the same nature as those provided for where the exceptions of contract or consent apply, and thus: "such measures should include as a minimum a way for the data subject to obtain human intervention, express their point of view, and contest the decision", noting that "human intervention is a key element".[57] Authorization by Member State law is nevertheless likely to result in significant divergence between national legislative regimes, which is not ideal given the Digital Single Market ideal pursued by the GDPR.

7.3 *Consent*

The third derogation listed in Article 22(2) concerns a decision based on the data subject's 'explicit' consent. Article 4(11) GDPR defines consent as "any freely given, specific, informed and unambiguous indication of the data subject's wishes by which he or she, by a statement or by a clear affirmative action, signifies agreement to the processing of personal data relating to him or her". Furthermore, Article 7 GDPR on the conditions for consent, provides that "When assessing whether consent is freely given, utmost account shall be taken of whether, *inter alia*, the performance of a contract, including the provision of a service, is conditional on consent to the processing of personal data that is not necessary for the performance of that contract or provision of that service".[58] It is, therefore, relevant to consider whether conditional automated decision-making is necessary for the performance of that contract. The data subject's interest in that contract is also relevant. For example, suppose the data subject applies for credit or insurance. In that case, the fact that the contract is in the data subject's interest makes it easier to argue that consent is freely given than when the decision is not.

7.4 *Safeguards*

In cases where the exceptions of contract and consent apply, the data controller must implement suitable safeguards, which must consist of at least the right to obtain human intervention on the part of the controller to express his or her point of view and to contest the decision.[59] Therefore, the data subject should always have the right to demand a human review of an automated decision. Mendoza and Bygrave posit that "these rights (particularly that of human involvement) mean that there will be insignificant difference in the level of

57 A29WP 2018 *Guidelines*, 27.
58 Article 7(4) GDPR; cf. recital (43).
59 Article 22(3) GDPR.

protection between the right/prohibition in Article 22(1) and the exceptions".[60] In a similar vein, Bygrave concludes that: "there will ultimately be very little difference between the level of protection offered by the exercise of the 'right' in Article 22(1) and that offered by the exercise of the rights in Article 22(3), particularly in the situation where the former 'right' is exercised *ex-post* (i.e. after a decision is adopted)".[61]

The list of essential safeguards found in Article 22(3) is not exhaustive; other safeguards may be implemented that are not listed there. In particular, whether a 'right to an explanation' of a particular decision is a safeguard that the GDPR mandates has been the subject of much debate and controversy.

8 A 'Right to an Explanation'?

The controversy surrounding the existence or otherwise of a 'right to an explanation' emerges from a reading of Article 22(3) in light of the recital (71), which provides that "such processing should be subject to suitable safeguards, which should include [the right] to obtain an explanation of the decision reached after such assessment". It should be recalled, however, that recitals have no binding legal force.[62] They are merely "interpretative tools in the EU legal order" that "help to explain the purpose and intent behind a normative instrument" and "can also be taken into account to resolve ambiguities in the legislative provisions to which they relate". Nevertheless, a recital "cannot displace the operative provisions of a legal instrument".[63]

This has resulted in considerable controversy over the question of the nature and existence of such a 'right to an explanation' under the GDPR.[64] If such a right exists, it is nevertheless unclear whether this right consists of an

60 Mendoza and Bygrave (n 18) 92.

61 Bygrave, *A Commentary* (n 44) 538.

62 Case C-162/97, Nilsson, [1998] ECLI:EU:C:1998:554, para 54.

63 Roberto Baratta, 'Complexity of EU law in the domestic implementing process' [2014] 19th Quality of Legislation Seminar – EU Legislative Drafting: Views from those applying EU law in the Member States <https://ec.europa.eu/dgs/legal_service/seminars/20140703_baratta_speech.pdf> references excluded, accessed 9 February 2023.

64 Brybe Goodman and Seth Flaxman, 'European Union Regulations on Algorithmic Decision-Making and a "Right to Explanation"' (2017) 38(3) AI Magazine 50 ('any adequate explanation would, at a minimum, provide an account of how input features relate to predictions …' at p. 29); Sandra Wachter, Brent Mittelstadt, and Luciano Floridi, 'Why a Right to Explanation of Automated Decision-Making Does Not Exist in the General Data Protection Regulation' (2017) 7 International Data Privacy Law 76; Andrew D Selbst and Julia Powles, 'Meaningful information and the right to explanation' (2017) 7(4) International Data Privacy Law 233.

explanation of specific decisions (*ex-post* explanation) or an explanation of system functionality. Moreover, uncertainty surrounds the question of the extent to which companies must disclose information about their algorithms and how this obligation is to be balanced with the company's right to intellectual property protection,[65] including trade secrets. Furthermore, the extent to which an ML operation and/or output can be explained at all is doubtful,[66] and it is, in any case, doubtful whether an overly complex explanation would comply with the principle of transparency.

Insofar as transparency is concerned, Article 13 of the GDPR provides that a controller is obliged to provide the data subject with specified information when personal data are obtained, where information is collected from a data subject. In particular, the controller must inform the data subject of "the existence of automated decision-making, including profiling, referred to in Article 22(1) and (4) and, at least in those cases, *meaningful information about the logic involved*, as well as the significance and the envisaged consequences of such processing for the data subject".[67] An identical information requirement is found in Article 14 of the GDPR, which provides information requirements where personal data have not been obtained from the data subject (but from a third party).[68] Both Articles 13 and 14 envisage the provision of this information at the time of processing and would thus seem to indicate that what is being envisaged is not a right to an explanation of a particular decision, and, because of the requirement to provide "meaningful information about the logic involved", "not necessarily a complex explanation of the algorithms used or disclosure of the full algorithm".[69]

Beyond Articles 13 and 14, Article 15 GDPR provides for the right of a data subject to have access to the personal data concerning him or her that are processed by a controller, including information concerning "the existence of automated decision-making, including profiling, referred to in Article 22(1) and (4) and, at least in those cases, meaningful information about the logic involved, as well as the significance and the envisaged consequences of such processing for the data subject".[70] While the data subject's right of access under Article 15 would be exercised after the processing has commenced,

65 See Art 17 Charter of Fundamental Rights of the European Union [2012] OJ C 326/391.

66 See EDPS, TechDispatch #2/2023 – Explainable Artificial Intelligence (16 November 2023) <https://www.edps.europa.eu/data-protection/our-work/publications/techdispatch/2023-11-16-techdispatch-22023-explainable-artificial-intelligence_en#:~:text=Explainable%20Artificial%20Intelligence%20(XAI)%20is,of%20their%20decision%2Dmaking%20processes> accessed 24 April 2024.

67 Art 13(2)(f) GDPR [author's emphasis].

68 Art 14(2)(g) GDPR.

69 A29WP 2018, 25.

70 Art 15(1)(h) GDPR.

the identical wording to that found in Articles 13 and 14 has led the A29WP to conclude that the interpretation of the equivalent element under Article 15 should be interpreted in the same way, and thus that there is no *ex post* right to an explanation of a particular decision. The fact that the provision speaks of "the significance and envisaged consequences" of the processing indicates that this is not an *ex-post* explanation of a particular decision.[71] Nevertheless, in the opinion of the A29WP, the controller should "provide the data subject with general information (notably, on factors taken into account for the decision-making process, and on their respective 'weight' on an aggregate level) which is also useful for him or her to challenge the decision".[72]

In line with the view of the A29WP, Mendoza and Bygrave posit that "we should not discount the possibility that a right of *ex-post* explanation of automated decisions is implicit in the right 'to contest' a decision pursuant to Article 22(3)".[73] If a data subject wants to contest a decision, at a minimum, they need to be heard and the merits of the contestation considered by the decision-maker. Such a process would not be fair if the decision-maker were not subject to a qualified obligation[74] to give reasons for (or an explanation of) the decision.[75] Furthermore, the obligation to give reasons is buttressed by the core data protection principle of "fairness, lawfulness and transparency", which is given effect in various GDPR provisions, including Article 22.

The AG Opinion in the *SCHUFA* case[76] reflects this author's conclusions based on the above considerations. In that case, *SCHUFA*, the credit information service provider, refused to disclose the various elements taken into account to calculate the creditworthiness assessment score and their weighting, referring to trade secrecy. The AG posited that Article 15(1)(h) must be interpreted as meaning that it covers, in principle, also the method of calculation used by a commercial information company to establish the credit score, provided that there are no conflicting interests worthy of protection. In this respect, the AG pointed towards recital (63) GDPR, which states that the right of access "should not adversely affect the rights or freedoms of others, including trade secrets or intellectual property and in particular the copyright protecting the software".[77] The AG opined that a 'fair balance' between competing interests must be sought. Moreover, recital (63) states that "the result of those

71 A29WP 2018, 27.
72 *Ibid.*
73 Mendoza and Bygrave (n 18) 93–94.
74 See Article 23 GDPR on restrictions to data subject rights.
75 Mendoza and Bygrave (n 18) 93–94.
76 C-634/21 *Shufa*, Opinion (n 19).
77 C-634/21 *Shufa*, Opinion (n 19) para 54.

considerations should not be a refusal to provide all information to the data subject". Reading Article 15(1)(h) in light of the transparency requirements of Article 12, and in particular that the data subject should receive information that is understandable and accessible, the AG excluded a possible obligation to disclose the algorithm, given its complexity, emphasizing that "the usefulness of communicating a particularly complex formula would be doubtful without providing the necessary explanations".[78] Thus the Article 15(1)(h) obligation:

> must be understood as meaning that it includes *sufficiently detailed explanations of the method used for the calculation of the score and the reasons that led to a particular result*. In general, the data controller should provide the data subject with aggregate information, in particular on the factors taken into consideration for the decision-making process and their respective importance at an aggregate level, which is also useful for him to challenge any "decision" in the sense of Article 22(1) GDPR.[79]

This line of interpretation was also previously upheld by the Amsterdam District Court, which required Ola to explain the logic behind a fully automated decision. That Court also referred to the A29WP Guidelines, interpreting Article 15(1)(h) to mean that "the main assessment criteria and their role in the automated decision" must be communicated to the data subjects "so that they can understand the criteria based on which the decisions were taken, and they can check the correctness and lawfulness of the data processing".[80]

Summarising, the position at law is as follows:

i. Requirement to disclose 'meaningful information' or an 'explanation' of system functionality that is sufficiently detailed as to enable a right to contest the decision as per Article 22(3);
ii. Coupled with a right of access to personal data processed relating to the data subject, an explanation of system functionality should lead to an explanation of the specific decision made;
iii. There is no requirement to disclose the algorithm;
iv. It requires a balancing of interests of the data subject and the controller (in particular, data protection and intellectual property-related interests).

78 *Ibid*., para 57.
79 *Ibid*., para 58 (emphasis added).
80 Amsterdam District Court, 11 March 2021, C / 13/689705 / HA RK 20-258, para 4.47 [unofficial English translations available <https://ekker.legal/en/2021/03/13/dutch-Court-rules-on-data-transparency-for-uber-and-ola-drivers/>] para 4.52.

9 Limitations of the 'Right to an Explanation'

The data subject's right to receive an explanation may be restricted per Article 23 of the GDPR.[81] As aforementioned, this may prevent undue prejudice to the rights and legitimate interests of the decision-maker, particularly regarding intellectual property rights, such as trade secrets. Nevertheless, the principle of transparency expounded in the recital (58) is highly relevant in "situations where the proliferation of actors and the technological complexity of practice make it difficult for the data subject to know and understand whether by whom and for what purpose personal data relating to him or her are being collected".

Thus, seeking a fair balance between competing rights and responsibilities is necessary, considering the fundamental nature of both data protection rights and intellectual property.[82] The Advocate General in the *SCHUFA* case considered that the obligation to provide "meaningful information about the logic involved" should be read in light of the aforementioned recitals and that:

> A minimum of information must in any case be provided in order not to compromise the essential content of the right to the protection of personal data. (…) [I]f the protection of trade secrecy or intellectual property constitutes, in principle, for a commercial information company a legitimate reason to refuse to reveal the algorithm used to calculate the score of the data subject, (…) it can in no way justify an absolute refusal of information. More so, when there are appropriate means of communication, which facilitate understanding while guaranteeing a certain degree of confidentiality'.[83]

10 Prohibitions of Decisions Based on "Special Categories of Personal Data"

Article 22(4) prohibits automated decision-making based on "special categories of personal data".[84] While this supersedes the exceptions listed in Article 22(2), it is a qualified prohibition as there are another two exceptions: if

81 Art 23(1)(i) GDPR.

82 Art 8 on the protection of personal data and Art 17 on the Right to property (including intellectual property) Charter of Fundamental Rights of the European Union.

83 C-634/21 *Shufa*, Opinion (n 19) para 56 (my translation).

84 Defined in Article 9(1) GDPR.

the data subject has given explicit consent to the processing of those personal data under Article 9(1)(a); and if the processing is necessary for reasons of substantial public interest under Article 9(1)(g). In the latter case, the processing must be provided for by Union or Member State law and be "proportionate to the aim pursued, respect the essence of the right to data protection and provide for suitable and specific measures to safeguard the fundamental rights and the interests of the data subject". Furthermore, "suitable measures to safeguard the data subject's rights, freedoms, and legitimate interests" must be in both cases. These requirements are identical in wording to those found in Article 22(2) and (3) and should thus presumably be interpreted similarly.

11 Rights for Groups and Society

Data protection legislation has emerged from a human rights paradigm, thus focusing mainly on individual rights. It is important, however, to acknowledge the limitations of the individual rights paradigm to consider rights for groups and society more broadly, as well as the tools in data protection law's arsenal that uphold such broader rights. Moreover, data protection law moves beyond its foundational concern with privacy-related interests to encompass concerns about averting discriminatory effects. This is evidenced in the text of a recital of the GDPR:

> the controller should use appropriate mathematical or statistical procedures for the profiling, implement technical and organisational measures appropriate to ensure, in particular, that factors which result in inaccuracies in personal data are corrected and the risk of errors is minimised, secure personal data in a manner that takes account of the potential risks involved for the interests and rights of the data subject, and prevent, *inter alia*, discriminatory effects on natural persons on the basis of racial or ethnic origin, political opinion, religion or beliefs, trade union membership, genetic or health status or sexual orientation, or processing that results in measures having such an effect.[85]

One might ponder the efficacy of exercising individual rights, like the 'right to an explanation', and question whether these rights truly offer a meaningful remedy across various situations. Furthermore, transparency is largely

85 Recital (71) GDPR.

inadequate for understanding and governing algorithmic systems, given the complexities of societal power dynamics and institutions, leading to potential societal or algorithmic harms. Hence, there is a need to guard against the 'transparency fallacy', wherein the anticipated advantages of apparent transparency prove illusory due to individuals being predominantly time – and resource-constrained and often lacking the requisite expertise to exercise these rights effectively.[86] Thus, it becomes essential to go beyond individual rights and shift our focus towards algorithmic governance.[87]

12 Impact Assessments

An impact assessment is an *ex-ante* systematic evaluation process used to analyse the potential consequences of a proposed action, policy, project, or decision on various social, environmental, economic, and legal factors. The GDPR establishes the mandatory requirement of carrying out a 'data protection impact assessment' (DPIA) in case of processing likely to result in a high-risk to data subjects: "Where a type of processing … is likely to result in a high risk to the rights and freedoms of natural persons, the controller shall, *prior* to the processing, carry out an assessment of the impact of the envisaged processing operations on the protection of personal data".[88] It is further specified that a DPIA is required in particular in the case of a systematic and extensive evaluation of personal aspects relating to natural persons, which is based on automated processing, including profiling, and on which decisions are based that produce legal effects concerning the natural person or similarly significantly affect the natural person'[89] and "processing on a large scale of special categories of data".[90] A DPIA proves invaluable in crafting the requisite safeguards in alignment with the stipulations outlined in Article 22 of the GDPR. Furthermore, where the DPIA indicates that the processing "would result in a high risk in the absence of measures taken by the controller to mitigate the risk", the

86 Edwards and Veale (n 14).

87 Mike Ananny and Kate Crawford, 'Seeing without knowing: Limitations of the transparency ideal and its application to algorithmic accountability' (2018) 20(3) New Media & Society 973.

88 Article 35(1) GDPR; See A29WP *Guidelines on Data Protection Impact Assessment* (*DPIA*) *and determining whether processing is "likely to result in a high risk" for the purposes of Regulation 2016/679* (wp248rev.01) Adopted on 4 April 2017 As last Revised and Adopted on 4 October 2017 <https://ec.europa.eu/newsroom/article29/items/611236/en>.

89 Art 35(3)(a) GDPR.

90 Art 35(3)(c) GDPR.

controller must consult the supervisory authority before the start of processing activities.[91] The supervisory authority would, in turn, be able to exercise its powers, including imposing a temporary or definitive limitation, such as a ban on processing.[92] Thus, a decisional system may be banned *ex-ante* (and fines imposed upon non-compliant controllers[93]).

A weakness of this requirement is that it is premised on the controller's self-assessment of the nature of the risk of the processing. Nevertheless, 'high-risk' technologies are almost certain to capture most predictive analytics or ML systems. However, one should also note that a DPIA is not a comprehensive *ex-ante* fundamental rights-based impact assessment; that is, a human rights impact assessment emphasising elements such as fairness, equality and non-discrimination. 'Algorithmic Impact Assessments' have been proposed to link individual rights and systemic governance,[94] thus providing algorithmic accountability. While not yet a requirement for all AI systems, this obligation is anticipated to be instituted for systems classified as 'high-risk' with the enactment of the AI Act.[95]

13 'By Design' Strategies

'By design' strategies refer to the deliberate incorporation of legal principles, safeguards, and mechanisms into the fundamental structure and development process of systems, products, or services to ensure compliance and mitigate risks from the outset. For example, 'data protection by design' entails integrating privacy and security measures into the development process of systems, products, or services from their inception. Article 25 of the GDPR provides an obligation for the controller to "implement appropriate technical and organisational measures, such as pseudonymisation, which are designed to implement data-protection principles, such as data minimisation, effectively and to integrate the necessary safeguards into the processing in order to meet the

91 Art 36(1) GDPR.

92 Art 58(2)(f) GDPR.

93 Art 83 GDPR.

94 Margot E Kaminski, Gianclaudio Malgieri, Algorithmic impact assessments under the GDPR: producing multi-layered explanations, *International Data Privacy Law*, Volume 11, Issue 2, April 2021, 125–144.

95 Proposal for a Regulation of the European Parliament and of the Council laying down harmonised rules on Artificial Intelligence (Artificial Intelligence Act) and amending certain Union legislative Acts COM/2021/206 final. The AI Act was formally adopted by Parliament on 13 March 2024.

requirements of this Regulation and protect the rights of data subjects". This obligation exists "both at the time of determining the means for processing and at the time of the processing itself".[96] The obligation imposed by Article 25 is qualified by an extensive list of contextual factors: "Taking into account the state of the art, the cost of implementation and the nature, scope, context and purposes of processing as well as the risks of varying likelihood and severity for rights and freedoms of natural persons posed by the processing". These will be determined largely by the data protection impact assessment that controllers engaging in processing that is "likely to result in a high risk" to persons' rights and freedoms are required to conduct according to Article 35 above. Thus, there is a link between impact assessments and Article 25 requirements.

14 Accountability: *Ex-ante* Impact Assessments, *Post-Factum* Audits and Effective Remedies

Through initiatives like impact assessments, 'by design' strategies, and others such as codes of conduct[97] and certification,[98] increased accountability for unfairness, discrimination, and reparations to affected individuals and communities are anticipated. However, some organizational difficulties need to be overcome. For instance, determining responsibility for reviewing audit trails raises questions about whether it should be assigned to an external regulator like the supervisory authorities established under the GDPR or an audit body. Moreover, implementing and enforcing such requirements in the private sector poses greater challenges. Further considerations include the risk of excessive bureaucratic burdens that do not translate into effective heightened substantive protection for data subjects.

15 Conclusion

This book chapter has explored the societal risks associated with automated individual decision-making, including profiling, and the rationale for its regulation through data protection legislation, particularly emphasising Article 22 of the GDPR and its role within the Internal Market. Through a critical analysis of this provision, drawing on interpretative case law such as the

96 Article 25 GDPR.
97 See Art 40 GDPR.
98 See Art 42 GDPR.

recent CJEU *SCHUFA* ruling, the chapter situates the regulation of automated decision-making within a broader context. It has considered other GDPR provisions to foster safe technological systems to prevent harm rather than solely providing retrospective remedies. These considerations have been central since the enactment of the GDPR in 2016, with evolving discourse. This discourse has culminated in the proposal for an AI Act, which, after a protracted legislative process, nears enactment. Notably, the AI Act introduces mandatory 'fundamental rights impact assessments'[99] and a 'right to an explanation of individual decision-making'[100] for 'high-risk' AI systems.[101] A discussion on the implications of the AI Act on the regulation of AI systems is beyond the scope of this chapter but is addressed in the following one.

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99 Art 27 AI Act.

100 Art 86 AI Act.

101 Defined in Art 6 AI Act.

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CHAPTER 6

Regulating Artificial Intelligence in the European Union

Mireille M. Caruana and Roxanne Meilak Borg

Abstract

The EU AI Act marks a significant milestone as the world's first comprehensive legal framework for Artificial Intelligence. This pioneering legislation aims to regulate AI systems' development, deployment, and use to foster innovation while ensuring safety, transparency, and adherence to fundamental rights. The chapter will analyse the AI Act in light of the underlying goal of 'regulation for innovation', which seeks to enhance the adoption of AI within the Internal Market by bolstering trust in technological advancements. The narrative provides an overview of the AI Act, outlining its framework and key components. It delves into the Act's adoption of a risk-based regulatory approach, which precludes AI systems that pose an unacceptable risk, heavily regulates AI systems that pose high risks, and lightly regulates systems posing limited risks. The chapter further explores other essential aspects of the Act, including regulating general-purpose AI models, requirements and obligations like conducting Fundamental Rights Impact Assessments, the role of standards and benchmarks, regulatory sandboxes, and the functions of the European AI Office and AI Board. These elements underscore the Act's potential to harmonise AI regulation within the Internal Market and influence the future landscape of AI in Europe and beyond. The discussion refers to the achievements and challenges faced by the EU legislator in creating a unified regulatory environment in light of the potential impacts on the Digital Single Market and the EU's competitiveness on the global stage. It assesses how the Act navigates the balance between fostering innovation and safeguarding fundamental rights. This chapter offers an overview of the AI Act, focusing on pivotal aspects of shaping the Internal Market and influencing global AI regulation frameworks. It also discusses the protection of fundamental rights within these regulatory structures.

1 Introduction

The uptake of AI systems has the potential to bring several individual and societal benefits and foster innovation and global competitiveness. While the

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industry does a great job promoting these benefits, we focus on AI's risks and potential harms in this chapter. AI systems are posed to generate various significant challenges and negative consequences, particularly through their impact on the democratic fabric of society, fundamental (or 'human') rights and other significant risks, including safety hazards when integrated into products and services. Thus, unregulated AI deployment may have irreversible negative consequences for humans and humanity; philosophers, lawyers, and others must discuss and debate the immensely important subject of regulating AI.

This chapter considers conversations about regulating AI, focusing on the legislative initiatives that have been, or are in the process of being, undertaken within the European Union ('EU').[1] In April 2021, the European Commission published a proposal for an EU regulatory framework on Artificial Intelligence. It was intended as future-proof legislation with flexible mechanisms that would allow it to adapt and evolve with new regulatory challenges and concerns. This proposal represents the first-ever attempt to enact a horizontal regulation of AI within the EU. The Council of the EU adopted its common position on such proposed legislation in December 2022,[2] and the European Parliament ('EP') in June 2023.[3] In December 2023, the Council and the EP reached a final political agreement on the text of the AI Act, which the EP has now passed.[4]

1 The Council of Europe recently adopted the first-ever international treaty on artificial intelligence, which will not, however, be considered in this chapter. For more information, see: <https://www.coe.int/en/web/portal/-/council-of-europe-adopts-first-international-treaty-on-artificial-intelligence> accessed 20 May 2024.

2 The Council adopted its common position ('Proposed AI Act (Council General Approach') on the AI Act on 6 December 2022: Proposal for a Regulation of the European Parliament and of the Council laying down harmonised rules on Artificial Intelligence (Artificial Intelligence Act) and amending certain Union legislative acts – EU Council General approach - Brussels, 25 November 2022 <https://data.consilium.europa.eu/doc/document/ST-14954-2022-INIT/en/pdf> accessed 20 May 2024. See also Artificial Intelligence Act: Council calls for promoting safe AI that respects fundamental rights, Press release 6 December 2022, <https://www.consilium.europa.eu/en/press/press-releases/2022/12/06/artificial-intelligence-act-council-calls-for-promoting-safe-ai-that-respects-fundamental-rights/> accessed 20 May 2024.

3 Amendments adopted by the EP on 14 June 2023 on the proposal for a regulation of the EP and of the Council on laying down harmonised rules on Artificial Intelligence (Artificial Intelligence Act) and amending certain Union legislative acts (COM(2021)0206 – C9-0146/2021 – 2021/0106(COD)) <https://www.europarl.europa.eu/doceo/document/TA-9-2023-0236_EN.pdf> accessed 17 May 2024.

4 The text of the final draft (European Parliament 'Corrigendum' of 16th April 2024) is available here: <https://www.europarl.europa.eu/doceo/document/TA-9-2024-0138-FNL-COR01_EN.pdf> accessed 17 May 2024. The Regulation is expected to be finally adopted before the end of the legislature and also needs to be formally endorsed by the Council.

The stated purpose of the Act is to improve internal market functioning through a uniform legal framework for the development, placing on the market, putting into service and use of AI systems in the Union to promote the uptake of human-centric and trustworthy AI while ensuring a high level of protection of health, safety, fundamental rights as enshrined in the EU Charter of Fundamental Rights, to protect against the harmful effects of AI systems in the Union, and to support innovation. The Act ensures the free movement, cross-border, of AI-based goods and services. It prevents Member States from imposing restrictions on the development, marketing and use of AI systems unless explicitly authorised by it.[5]

The AI Act thus has a dual concern and relative function: free trade/elimination of trade barriers and individual and societal impact/protection of health, safety and fundamental rights. It is based on Article 114 of the Treaty on the Functioning of the European Union ('TFEU'), the 'internal market clause'. However, to the extent that it contains specific rules on the protection of individuals about the processing of personal data concerning restrictions of the use of AI systems for (i) remote biometric identification for law enforcement, (ii) risk assessments of natural persons for law enforcement and (iii) biometric categorisation for law enforcement, and in as far as those specific rules are concerned, the Act is based on Article 16 TFEU (the right to the protection of personal data).[6]

The Act will apply to private and public entities, regardless of their location within or outside the EU, as long as the AI system is available in the Union market or its use affects people in the EU. Among the Act's most important elements are the requirement of transparency and the need for rigorous safety checks before an AI system is released into the public domain. The broad shape of things to come in Europe has been set. However, this is continually being challenged and impacted by scientific and technological developments in the sector that the law sets out to regulate, such as the emergence during the legislative process of heightened debate and controversy surrounding regulating generative AI as a result of the public availability of 'large language models' ('LLMs') like ChatGPT.

This chapter will provide an overview and commentary on the AI Act's regulatory strategies and general structure. An article-by-article analysis of the Act is beyond the scope of this book chapter. Rather, we seek to shine a light on selected fundamental aspects of the legislation. The chapter proceeds as

5 Recital (1) AI Act.
6 Recital (3) AI Act.

follows: it first considers the subject matter that we are discussing regulating ('Artificial Intelligence Systems') insofar as necessary to make sense of the discussion that ensues. It then highlights the 'why' of regulating, or in other words, what fears and legal and/or other factors have driven the EU to regulate rather than allow market forces free rein. It clarifies why regulation is necessary to move on to a discussion of 'how' we should regulate. Here, the focus is on the 'risk-based' approach adopted by the European Union, which calibrates the regulatory burden to the gravity or likelihood of the (anticipated) risk or threat. Laws lay down rights and obligations; Product safety-type laws such as the AI Act mostly lay down obligations. Hence, it is necessary to consider 'who' is subject to these obligations (providers, deployers, importers, distributors, etc.) carefully. The discussion then proceeds to the substantive obligations imposed upon these actors. Given the technical nature of the field, the limits of law are evident. Thus, co-regulation plays a role, particularly for standards, the standardisation bodies that set them, and relative certification. The chapter outlines the governance and enforcement structures that the Act sets up and assesses their likelihood of effectiveness. It also considers the strategy and role of so-called 'AI regulatory sandboxes' and concludes with thoughts on the 'regulatory balance' that is sought between protection, technological development and innovation and the likelihood of the EU achieving this delicate balance.

2 Regulate What? Defining 'AI systems'

The AI Act regulates 'AI systems', defining an AI system as one that is 'machine-based', 'designed to operate with varying levels of autonomy and that may exhibit adaptiveness after deployment, and that, for explicit or implicit objectives, infers, from the input it receives, how to generate outputs such as predictions, content, recommendations, or decisions that can influence physical or virtual environments'.[7] The Council's General Approach on the Act narrowed the definition to systems developed through machine learning approaches and logic – and knowledge-based approaches;[8] this position was later abandoned,[9] and a technologically-neutral definition made it to the final draft text.

The debate on LLMs paved the way for the regulation by the Act of 'general-purpose' AI (GPAI) models and 'general-purpose' AI (GPAI) systems, which

7 Article 3(1) AI Act.

8 Article 3(1) Proposed AI Act (Council General Approach).

9 EP DRAFT Compromise Amendments 16 May 2023.

were not covered by the Commission's original proposal. The Act now includes a definition for both these terms, as follows:

> A 'general-purpose AI (GPAI) model' means "an AI model, including where such an AI model is trained with a large amount of data using self-supervision at scale, that displays significant generality and is capable of competently performing a wide range of distinct tasks regardless of the way the model is placed on the market and that can be integrated into a variety of downstream systems or applications, except AI models that are used for research, development or prototyping activities before they are placed on the market";[10]
>
> A 'general-purpose AI (GPAI) system' means "an AI system which is based on a general-purpose AI model and which has the capability to serve a variety of purposes, both for direct use as well as for integration in other AI systems".[11]

The definition of a GPAI model is broad. It is so broad that it has been argued that it could "be interpreted in such a way as to potentially include a vast variety of technological cases".[12] Typical examples of GPAI models are generative AI models[13] such as LLMs. These models are a tool for processing and generating natural language and have many potential applications in language translation, content generation, and conversational AI. They use deep learning, which involves training a neural network on vast amounts of textual data, such as books, articles, and web pages. An LLM aims to learn the patterns and relationships between words and phrases in natural language to generate coherent and meaningful text. This involves analysing the syntax and semantics of language and understanding the context in which words are used. ChatGPT-4, developed by OpenAI and released on the public web in March 2023, is one of the most well-known examples of LLMs.

LLMs can be considered a broader category encompassing foundation models. This type serves as a starting point for building other, more specialised models and constitutes an example of a general-purpose AI system. The term

10 Article 3(63) AI Act.

11 Article 3(66) AI Act.

12 Innocenzi Genna, 'Foundation Models: how they are regulated in the AI ACT' (*radiobruxelleslibera*, 5 February 2024) <https://radiobruxelleslibera.com/2024/02/05/foundation-models-how-they-are-regulated-in-the-ai-act/#:~:text=Foundation%20Models%20are%20now%20defined,components%20into%20an%20AI%20system> accessed 20 May 2024.

13 Recital (99) AI Act.

'foundation model' refers to the fact that these models provide a foundation of knowledge and understanding of language that can be used to build other, more specialised models for specific natural language processing ('NLP') tasks. For example, a foundation model could be fine-tuned on a smaller text dataset for a specific task, such as sentiment analysis or question answering, and then used to make predictions or generate text in that domain. The European legislator has chosen not to limit the provisions of the Act to 'foundation models'; these fall within the broader notions of LLMs and GPAI models.

Emily M. Bender has coined the term 'stochastic parrots' for LLMs,[14] which is now commonly used when referring to such models because, while impressive in their ability to generate natural language, they ultimately do not understand the meaning of the language they are processing (they just 'parrot'). LLMs are incapable of true reasoning or understanding; they merely rely on statistical patterns in data to generate responses. As a result, they are prone to errors and biases, as they can perpetuate stereotypes and other problematic patterns in language. Furthermore, they are not always transparent about how they arrive at their responses.[15] The output of "hallucinations", or made-up answers, has indeed triggered a GDPR-based complaint by NOYB against OpenAI (the company that has developed ChatGPT) on account of the output of false information about people and the inability or unwillingness of OpenAI to comply with the data access request and in so doing be transparent about their training data.[16]

3 Why Regulate? Threats to Fundamental Rights and Values

While there is no doubt about the promise of AI to make things better, the drive for regulation stems from certain fears relating to the development and deployment of AI systems, combined with a perceived insufficiency of

14 Emily M. Bender and others, 'On the Dangers of Stochastic Parrots: Can Language Models Be Too Big?' (2021) Proceedings of the 2021 ACM Conference on Fairness, Accountability, and Transparency 610 <https://doi.org/10.1145/3442188.3445922> accessed 20 May 2024.

15 Explained simply here: Muhammad Saad Uddin, 'Stochastic Parrots: A Novel Look at Large Language Models and Their Limitations' (*Towards AI*, 20 April 2023) <https://towardsai.net/p/machine-learning/stochastic-parrots-a-novel-look-at-large-language-models-and-their-limitations#:~:text=At%20its%20core%2C%20the%20term,the%20language%20they%20are%20processing> accessed 20 May 2024.

16 NOYB, 'ChatGPT provides false information about people, and OpenAI can't correct it' (*noyb,* 29 April 2024) <https://noyb.eu/en/chatgpt-provides-false-information-about-people-and-openai-cant-correct-it> accessed 20 May 2024.

current laws and ethical frameworks to protect against these feared harmful or otherwise negative consequences for individuals and/or for society. At the most extreme, concerns have been expressed that AI threatens to enslave or even exterminate us[17] or that future developments will mean that 'enslaving' AI will amount to nothing less than another form of modern-day slavery.[18]

A more nuanced viewpoint (embraced by these authors) holds that AI, a creation of humans, will be controlled by (some) humans, but its deployment may result in the enslavement of others. However, since (some) humans control its development, AI could be developed to protect fundamental or human rights and values 'by design'.

The AI Act refers to the "risk of harm to the health and safety, or an adverse impact on fundamental rights".[19] As expressed succinctly by the RAILS,

> AI systems have the potential to unpredictably harm people's life, health, and property. They can also affect fundamental values on which western societies are founded, leading to breaches of fundamental rights of people, including the rights to human dignity and self-determination, privacy and personal data protection, freedom of expression and assembly, non-discrimination, or the right to an effective judicial remedy and a fair trial, as well as consumer protection.[20]

Indeed, certain AI systems may be deemed to pose such a serious risk that they should not merely be regulated but banned outright. For example, the advocacy advisor on AI Regulation at Amnesty International has expressed the opinion that:

> The EU must ban the use of discriminatory AI systems which disproportionately affect people from marginalised communities, including

17 As reflected in science fiction in the Terminator series of films or in Isaac Asimov's I, Robot. See also: Nick Bostrom, *Superintelligence: Paths, Dangers, Strategies* (OUP 2014); Chris Vallance, 'Artificial Intelligence could lead to extinction, experts warn' (*BBC News,* 31 May 2023) <https://www.bbc.com/news/uk-65746524> accessed 20 May 2024.

18 Andrew Murray, 'When machines become sentient, we will have to consider them an intelligent life form' (*LSE*, 10 August 2018) <https://blogs.lse.ac.uk/businessreview/2018/08/10/when-machines-become-sentient-we-will-have-to-consider-them-an-intelligent-life-form/> accessed 20 May 2024.

19 Article 7(1)(b) AI Act.

20 Martin Ebers and others, 'The European Commission's Proposal For An Artificial Intelligence Act—A Critical Assessment By Members Of The Robotics And AI Law Society (RAILS)' (2021) 4(4) Multidisciplinary Scientific Journal (2021) <https://www.mdpi.com/2571-8800/4/4/43> accessed 5 May 2023.

> migrants, refugees and asylum seekers. Such technologies profile people and communities, claiming to 'predict' crimes or 'identify' people who supposedly pose a security risk, even leading to them being denied the right to asylum. EU lawmakers must not miss this opportunity to prohibit the use of certain AI-based practices and protect the rights of migrants, refugees, and asylum seekers against harmful aspects of AI.
>
> Use of mass surveillance technologies, such as retrospective and live remote biometric identification tools must also be banned. The proposed law must also ban discriminatory social scoring systems that prevent people from accessing essential public and private services, such as child support benefits and education.[21]

In this vein, the AI Act does prohibit certain AI practices. It considers, among others, that "AI systems providing social scoring of natural persons by public or private actors may lead to discriminatory outcomes and the exclusion of certain groups. …"[22]

AI is broad enough to include environments many of us already interact with daily, such as technology-powered search engines or social networking sites. Manipulative and/or deceptive practices may significantly impact individuals and societies; for example, digital nudging techniques exploit human vulnerabilities and the methods used by social media to make them addictive and keep users glued to the screen for as long as possible.[23]

Apart from the addictive element, the potential manipulation of online platforms ('intentional manipulation of their service, including by inauthentic use or automated exploitation of the service, as well as the amplification and potentially rapid and wide dissemination of illegal content and of information that is incompatible with their terms and conditions, to use the language of

21 Mher Hakobyan, Advocacy Advisor on Artificial Intelligence Regulation at Amnesty International, quoted in 'EU: European Union must protect human rights in upcoming AI Act vote' 26 April 2023 <https://www.commondreams.org/newswire/eu-european-union-must-protect-human-rights-in-upcoming-ai-act-vote> accessed 27 April 2023.

22 Recital (31) AI Act.

23 Tina van der Linden, 'Regulating Artificial Intelligence: Please Apply Existing Regulation' (Amsterdam Law Forum 2021) <https://www.amsterdamlawforum.org/articles/abstract/432>. Action against addictive design is part of formal proceedings opened by the Commission against TikTok in February 2024: European Commission, 'Commission opens formal proceedings against TikTok under the Digital Services Act' (*European Commission,* 19 February 2024) <https://ec.europa.eu/commission/presscorner/detail/en/ip_24_926> accessed 15 May 2024.

the Digital Services Act[24]), coupled with the practice of behaviourally targeted advertising, has various facets, not least their potential to influence elections and thus threaten an essential aspect of our democracies. A sustained focus on the detrimental impact of fake news and disinformation, coupled with harnessing the strengths of technology to target 'news' or political advertising in a particular way, started around the time of the Cambridge Analytica scandal, the British consulting firm that collected personal data belonging to millions of Facebook users without their consent, predominantly to be used for political advertising, and that was allegedly determinative of the election of Donald Trump as President of the United States, and the 'Brexit' referendum vote for the United Kingdom to leave the European Union.

Beyond the spread of disinformation, 'filter bubbles' – an algorithmic bias that skews or limits the information an individual user sees on the Internet – are also problematic for democratic discourse, as it means that an individual's online experience is not open to alternative, contrasting viewpoints to those already held.[25]

Thus, search engines and digital platforms such as social media platforms can have a deleterious impact at both the individual and the societal levels, threatening individual autonomy and dignity, as well as the democratic fabric of society and the rule of law. These developments in our online life experiences directly result from the profit-making target of the big businesses behind them.

It is important to protect fundamental rights in all situations. It has been argued that fundamental human rights can or should not be treated and evaluated equally with business (that is, profit) interests.[26] However, this is not to say that the freedom to conduct a business should not be considered.[27] The matter with AI is that, like other tools, it can be used for good or for bad. It can

24 Article 34(2) Regulation (EU) 2022/2065 of the European Parliament and of the Council of 19 October 2022 on a Single Market For Digital Services and amending Directive 2000/31/EC (Digital Services Act) OJ L 277/1

25 Eli Pariser, *The filter bubble: How the new personalized web is changing what we read and how we think* (Penguin, 2011); Paula Johanson, *Online Filter Bubbles* (Greenhaven Publishing, 2017).

26 Fanny Hidvegi, Daniel Leafier and Estelle Massey, 'The EU should regulate AI on the basis of rights, not risks (*Access Now*, 17 February 2021) <https://www.accessnow.org/eu-regulation-ai-risk-based-approach/> accessed 22 May 2023.

27 Article 16 EU Charter; Peter Craddock Op-Ed: Who dares question the primacy of data protection? 7 May 2024 <https://www.linkedin.com/pulse/op-ed-who-dares-question-primacy-data-protection-peter-craddock-kfkxe/?trackingId=xYW%2BEJ2RRjyEbnNgn8Lfsw%3D%3D> accessed 17 May 2024.

play a role in tackling environmental challenges,[28] but it can also contribute to them;[29] it can be used to protect and uphold fundamental rights, including human dignity, or to undermine them.[30]

4 How to Regulate? A 'Risk-Based' Approach

The AI Act adopts a 'risk-based' approach and lays down a 'horizontal' (as opposed to sector-specific) legal framework for AI that aims to ensure legal certainty; this is desirable as regulating all AI systems in an equally heavy-handed manner would arguably suppress innovation and merely help to strengthen the already dominant market players.[31] However, the difficulty in applying such an approach lies in deciding how or according to the criteria 'high-risk' to be determined. It has been suggested that initial criteria must be developed for assessing what is 'high risk' – thus determining whether an obligation to proceed to a full impact assessment is triggered.[32]

The Act does not, however, include any such criteria. It merely precludes AI systems that pose an unacceptable risk, listing several prohibited practices. Thus, it identifies and heavily regulates AI systems with high risks and briefly mentions systems with limited risks. It also includes a new Chapter V on general-purpose AI ('GPAI') models, which speaks of GPAI models with

28 See for example UNEP, 'How Artificial Intelligence is helping tackle environmental challenges' (*UNEP*, 7 November 2022) <https://www.unep.org/news-and-stories/story/how-artificial-intelligence-helping-tackle-environmental-challenges> accessed 29 May 2023.

29 See for example Annette Ekin, 'AI can help us fight climate change. But it has an energy problem, too' (*Horizon,* 12 September 2019) <https://ec.europa.eu/research-and-innovation/en/horizon-magazine/ai-can-help-us-fight-climate-change-it-has-energy-problem-too> accessed 29 May 2023.

30 European Union Agency for Fundamental Rights, Getting the Future Right: Artificial Intelligence and Fundamental Rights, 2020 <https://fra.europa.eu/sites/default/files/fra_uploads/fra-2020-artificial-intelligence_en.pdf> accessed 29 May 2023.

31 Cf. Thomas Höppner and Luke Streatfeild, 'ChatGPT, Bard & Co.: An Introduction to AI for Competition and Regulatory Lawyers' (2023) 9 Hausfeld Competition Bulletin (1/2023), Article 1, Available at SSRN <https://ssrn.com/abstract=4371681> or <http://dx.doi.org/10.2139/ssrn.4371681> Accessed 5 June 2023.

32 Lilian Edwards, Expert Opinion: Regulating AI in Europe – Four problems and four solutions, 31 March 2022 Ada Lovelace Institute <https://www.adalovelaceinstitute.org/wp-content/uploads/2022/03/Expert-opinion-Lilian-Edwards-Regulating-AI-in-Europe.pdf> accessed 31 May 2023.

'systemic risk' and ones "released under a free and open-source licence".[33] Each category mentioned in this paragraph is discussed in further detail below.

4.1 *Prohibited AI Practices*

The AI Act prohibits eight practices deemed to present unacceptable risks. These relate to manipulation, social scoring, the assessment of the risk of an individual committing a criminal offence, the compilation of facial recognition databases through untargeted data scraping, the inference of emotions in workplaces or education institutions, biometric categorisation systems and 'real-time' remote biometric identification ('RBI').[34]

Thus, the Act prohibits the placing on the market, putting into service, or use of an AI system:

1. That "deploys subliminal techniques beyond a person's consciousness or purposefully manipulative or deceptive techniques, with the objective, or the effect of materially distorting the behaviour of a person or a group of persons by appreciably impairing their ability to make an informed decision, thereby causing them to take a decision that they would not have otherwise taken in a manner that causes or is reasonably likely to cause that person, another person or group of persons significant harm";[35]
2. That "exploits any of the vulnerabilities of a natural person or a specific group of persons due to their age, disability or a specific social or economic situation, with the objective, or the effect, of materially distorting the behaviour of that person or a person belonging to that group in a manner that causes or is reasonably likely to cause that person or another person significant harm";[36]
3. For "the evaluation or classification of natural persons or groups of persons over a certain period based on their social behaviour or known, inferred or predicted personal or personality characteristics", with the social score leading to the detrimental or unfavourable treatment of certain natural persons or groups of persons that is unjustified or disproportionate to their social behaviour or its gravity, and/or in social contexts that are unrelated to the contexts in which the data was originally generated or collected;[37]

33 Article 53(2) AI Act.
34 Article 5 AI Act.
35 Article 5(1)(a) AI Act.
36 Article 5(1)(b) AI Act.
37 Article 5(1)(c) AI Act.

4. For "making risk assessments of natural persons in order to assess or predict the risk of a natural person committing a criminal offence, based solely on the profiling of a natural person or on assessing their personality traits and characteristics",[38] although this prohibition does not apply to systems "used to support the human assessment of the involvement of a person in a criminal activity, which is already based on objective and verifiable facts directly linked to a criminal activity";[39]
5. That "create or expand facial recognition databases through the untargeted scraping of facial images from the internet or CCTV footage";[40]
6. To "infer emotions of a natural person in the areas of workplace and education institutions, except where the use of the AI system is intended to be put in place or into the market for medical or safety reasons";[41] and
7. That "categorise individually natural persons based on their biometric data to deduce or infer their race, political opinions, trade union membership, religious or political beliefs, sex life or sexual orientation"[42] ('biometric categorisation systems'); this prohibition does not cover any labelling or filtering of lawfully acquired biometric datasets, such as images, based on biometric data or categorising of biometric data in the area of law enforcement.

The Act also prohibits the use of 'real-time' RBI systems in publicly accessible spaces for law enforcement unless and in so far as such use is strictly necessary for certain objectives as further specified by it.[43] In such latter cases, RBI systems must be deployed "only to confirm the identity of the specifically targeted individual", "be authorised by national law", and "comply with necessary and proportionate safeguards and conditions" about their use by such national law. Furthermore, the relevant law enforcement authority must have completed a fundamental rights impact assessment concerning the RBI system and registered it in the EU database.[44]

Each use of an RBI system for law enforcement requires a prior authorisation granted by a judicial authority or by an independent administrative authority "whose decision is binding of the Member State in which the use is to take

38 Article 5(1)(d) AI Act.
39 Ibid.
40 Article 5(1)(e) AI Act.
41 Article 5(1)(f) AI Act.
42 Article 5(1)(g) AI Act.
43 Article 5(1)(h)(i) – (iii) AI Act.
44 Article 5(2) AI Act.

place".[45] Such use must also be "notified to the relevant market surveillance authority ('MSA') and the national data protection authority",[46] which shall submit 'annual reports' on such use to the Commission.[47] The Commission's original proposal listed four prohibited AI practices (points 1, 2, 3 and 8 above). The other four practices were added further to the trilogue negotiation proceedings. As is evident from the law's wording, the prohibitions in points 1, 2, 3 and 5 are absolute, while some exceptions are permissible from those described in points 4, 6, 7 and 8 in the prescribed circumstances.

Apart from including some new prohibited practices, some changes have also been made to the wording of the original four provisions. For instance, the provision prohibiting the use of AI systems that exploit individuals' vulnerabilities has been extended to cover persons vulnerable due to their social or economic situation, where it previously only covered "age, physical or mental disability", and the prohibition of using AI for social scoring now also covers private actors, where it previously only applied to public authorities. Likely, the provision prohibiting the compilation of facial recognition databases through the untargeted scraping of online and CCTV footage was introduced due to the heightened awareness resulting from the Clearview AI and PimEyes cases.[48] The final draft text also saw an increase in the requirements to be fulfilled for the lawful use of RBI systems in publicly accessible spaces for law enforcement purposes, including having a national law authorising such use, conducting a fundamental rights impact assessment, registering such systems in an EU database, and notifying their use to additional competent authorities such as data protection authorities. This more stringent approach attempts to strike a balance between the exigencies of the law enforcement sector and the resistance of civil society, witnessed through the public consultation process,[49] as

45 Article 5(3) AI Act.

46 Article 5(4) AI Act.

47 Article 5(6) AI Act.

48 See for instance, Kashmir Hill, 'A Face Search Engine Anyone Can Use is Alarmingly Accurate' *The New York Times* (New York, 26 May 2022) <https://www.nytimes.com/2022/05/26/technology/pimeyes-facial-recognition-search.html> accessed 20 May 2024.

49 See for instance Amnesty International 'Europe: Proposed legislation too weak to protect us from dangerous AI systems' (21 April 2021) <https://www.amnesty.org/en/latest/press-release/2021/04/eu-legislation-to-ban-dangerous-ai-may-not-stop-law-enforcement-abuse/> accessed 20 May 2024 and SHERPA, 'Feedback to the European Commission on its Proposal for a legal act of the European Parliament and the Council laying down requirements for Artificial Intelligence' (6 August 2020) <https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12527-Artificial-intelligence-ethical-and-legal-requirements/F2665582_en> accessed 20 May 2024. All documentation

well as the opinion expressed by the European Data Protection Board ('EDPB') and the European Data Protection Supervisor ('EDPS'), which jointly called for a general ban on any use of AI for automated recognition of human features in publicly accessible spaces – such as of faces but also of gait, fingerprints, DNA, voice, keystrokes and other biometric or behavioural signals – in any context.[50] Finally, it is worth noting that the AI Act prohibits only the 'use' – and not the 'placing on the market' – of 'real-time' RBI systems. Thus, EU vendors can sell biometric systems that would be illegal to use in the EU for regimes in third countries.[51]

4.2 *High-Risk AI Systems*

'High-risk' AI systems are dealt with in Chapter III of the Act, which provides for the classification of and requirements for such systems, the obligations incumbent on providers and deployers, and standards for such systems. This section focuses on the classification of AI systems as 'high-risk'.

An AI system is classified as high-risk under the Act if: (i) it is itself a product or a safety component of a product covered by certain Union health and safety harmonisation legislation (listed in Annex I, such as toys, machinery, lifts or medical devices) and it is required to undergo a third-party conformity assessment in order to be placed on the market or put into service according to such legislation[52] or (ii) it falls within a category listed in Annex III.[53] The areas set out in this Annex are the following: biometrics; critical infrastructure; education and vocational training; employment, workers management and access to self-employment; access to and enjoyment of essential private services and essential public services and benefits; law enforcement; migration, asylum and border control management; administration of justice and democratic processes.

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submitted to the Commission pursuant to the public consultation period are available at <https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12527-Artificial-intelligence-ethical-and-legal-requirements/feedback_en?p_id=24212003> accessed 20 May 2024.

50 EDPB-EDPS Joint Opinion 5/2021 on the proposal for a Regulation of the European Parliament and of the Council laying down harmonised rules on Artificial Intelligence (Artificial Intelligence Act) 18 June 2021.

51 Michael Veale and Frederik Zuiderveen Borgesius, 'Demystifying the Draft EU Artificial Intelligence Act' (2021) 22(4) Computer Law Review International 101.

52 Article 6(1) AI Act.

53 Article 6(2) AI Act.

Notably, an AI system that falls within any of these categories but "does not pose a significant risk of harm to the health, safety or fundamental rights of natural persons, including by not materially influencing the outcome of decision-making" because it is intended to "perform a narrow procedural task", "improve the result of a previously-completed human activity", "detect decision-making patterns or deviations from prior decision-making patterns and not meant to replace or influence the previously completed human assessment, without proper human review" or "perform a preparatory task to an assessment relevant for the use cases listed in Annex III" is not considered to constitute a high-risk system.[54] An embryonic version of this provision exempting AI systems that are unlikely to cause significant risk to the health, safety or fundamental rights was first introduced by the Council in its General Approach.[55] On the other hand, AI systems that perform profiling of natural persons shall "always be considered to be high-risk".[56]

The Commission can amend the list in Annex III through delegated acts. The Commission may include sub-areas within the existing ones if the AI system poses risks similar to those of an existing in-scope AI system, but cannot add entirely new areas.[57] Under a provision introduced by the Council's General Approach,[58] the Commission may remove high-risk AI systems from the list, provided such systems no longer pose significant risks to fundamental rights, health or safety.[59]

4.3 *Limited Risk AI Systems*

'Limited risk' AI systems are subject to transparency obligations in certain circumstances for providers and users of certain AI systems (chatbots, biometric categorisation, emotion recognition system, 'deep fakes'), so users know they are interacting with a machine.[60] For example, Article 50 *inter alia* provides that:

> Providers shall ensure that AI systems intended to interact directly with natural persons are designed and developed in such a way that the natural persons concerned are informed that they are interacting with an AI

54 Article 6(3) AI Act.
55 Article 6(3) Proposed AI Act (Council General Approach).
56 Article 6(3) AI Act.
57 Article 7 AI Act.
58 Article 7(3) Proposed AI Act (Council General Approach).
59 Article 7(3) AI Act.
60 Article 50 AI Act.

> system, unless this is obvious from the point of view of a natural person who is reasonably well-informed, observant and circumspect, taking into account the circumstances and the context of use. (...)[61]

4.4 *Minimal Risk AI Systems*

The AI Act allows other types of applications to be legally developed. This could include applications such as AI-enabled video games or spam filters. Article 95, on "codes of conduct for voluntary application of specific requirements", is the only relevant provision.

4.5 *General-Purpose AI Models*

General-purpose AI (GPAI) models are regulated in Chapter V of the Act, distinguishing between generic GPAI models, GPAI models "with systemic risk", and "free and open-source licence" GPAI models.

A GPAI model is classified as one with systemic risk[62] if (a) it has high-impact capabilities evaluated based on appropriate technical tools and methodologies, including indicators and benchmarks, *or* (b) based on a decision of the Commission, *ex officio* or following a qualified alert from the scientific panel, it has capabilities or an impact equivalent to those set out in point (a) having regard to the criteria set out in Annex XIII of the Act.[63]

GPAI models with systemic risk classified as such under (a) above must be notified to the Commission.[64] If the Commission becomes aware of a GPAI model with systemic risk of which it has not been notified, it may designate it as such.[65] It is also possible for the provider of a GPAI model that meets this condition to argue that, exceptionally, such a model does not, in fact, due to its specific characteristics, present systemic risks and, therefore, should not be classified as such. However, the Commission may reject these arguments.[66] A designation decision may be changed upon a reasoned request by a provider and if accepted by the Commission.[67] A list of GPAI models with systemic risk must be published and updated by the Commission (without prejudice

61 Article 50(1) AI Act.
62 Defined in Art. 3(65) AI Act.
63 Article 51(1) AI Act.
64 Article 52 AI Act.
65 Ibid.
66 Article 52(3) AI Act.
67 Article 52(5) AI Act.

to intellectual property rights and confidential business information or trade secrets).[68]

These provisions represent a change from the Council's position, where GPAI systems to be used as high-risk AI systems or components of such systems would have had to comply with the requirements for high-risk AI systems.[69] The final version of the Act has introduced the notion of GPAI models with systemic risk, and GPAI models must comply with the new Chapter V and all other relevant obligations within the Act.

5 Regulate Who? Providers v Deployers

When regulating Artificial Intelligence, a central question is who should be subjected to legal requirements, obligations and potential future liability. The developer – or, in the language of the AI Act, 'provider' – is the entity that will have the knowledge and practical control of the training sets, algorithms, etc. It may be argued that developers should carry legal responsibility, as the high-risk obligations mostly arise at the development stage. Such an argument is strengthened when the developer significantly profits from licensing their product or service. However, a counter-argument about GPAI notes that provider responsibility (and potential subsequent liability) may not include responsibility/liability for unforeseeable uses/risks. Nevertheless, it may not be practical (or even fair) to impose certain obligations on deployers because it may be impossible for them to fix or even audit issues of data quality, etc without access to the upstream source code, training datasets etc (which are often secret/proprietary, as with ChatGPT 4). Previous versions of the Act were also criticised for not reflecting the actors in the AI ecosystem accurately;[70] the final version has clarified the taxonomy of such entities – including, for instance, replacing the previously-employed term of 'user' with 'deployer' – and bestows responsibilities and obligations on various actors.

68 Article 52(6) AI Act.

69 Article 4b Proposed AI Act (Council General Approach).

70 See for instance Norberto Nuno Gomes de Andrade, Laura Galindo and Antonella Zarra, 'Artificial Intelligence Act: A Policy Prototyping Experiment. Revisiting the Taxonomy of AI Actors' (*Open Loop*, April 2023) <https://openloop.org/programs/open-loop-eu-ai-act-program/?utm_source=substack&utm_medium=email> accessed 8 May 2023.

The Act regulates both public and private actors. It applies to:

a. providers placing on the market or putting into service AI systems or placing on the market general-purpose AI models in the Union, irrespective of whether those providers are established or located within the Union or in a third country;
b. deployers of AI systems that have their place of establishment or are located within the Union;
c. providers and deployers of AI systems that have their place of establishment or are located in a third country, where the output produced by the system is used in the Union;
d. importers and distributors of AI systems;
e. product manufacturers placing on the market or putting into service an AI system together with their product and under their name or trademark;
f. authorised representatives of providers, which are not established in the Union;
g. affected persons that are located in the Union.[71]

The entities listed above are defined as follows:

A 'provider' is "a natural or legal person, public authority, agency or other body that develops an AI system or a general-purpose AI model or that has an AI system or a general-purpose AI model developed and places it on the market or puts the AI system into service under its name or trademark, whether for payment or free of charge".[72] A 'deployer' is "a natural or legal person, public authority, agency or other body using an AI system under its authority, except where the AI system is used during a personal, non-professional activity".[73] An 'authorised representative' is "a natural or legal person located or established in the Union who has received and accepted a written mandate from a provider of an AI system or a general-purpose AI model to respectively, perform and carry out on its behalf the obligations and procedures established by this Regulation".[74] An 'importer' is "any natural or legal person located or established in the Union that places on the market an AI system that bears the name or trademark of a natural or legal person established in a third country".[75] A 'distributor' is "any natural or legal person in the supply chain, other

71 Article 2(1) AI Act.
72 Article 3(2) AI Act.
73 Article 3(4) AI Act.
74 Article 3(5) AI Act.
75 Article 3(6) AI Act.

than the provider or the importer, that makes an AI system available on the Union market".[76] An 'operator' is "a provider, product manufacturer, deployer, the authorised representative, importer or distributor".[77]

6 Regulate How? (Requirements and Obligations)

This section first describes the requirements for high-risk AI systems and the obligations of providers and deployers of such systems as laid out in Chapter III, Sections 2 and 3 and Chapter IX, Sections 1 and 2 of the AI Act. Then, it moves on to the obligations of providers of GPAIs listed in Chapter V, Sections 2 and 3. Additional specific transparency obligations, incumbent on providers and deployers and set out in Chapter IV of the Act, are discussed in a subsequent section below.

6.1 *Requirements and Obligations for High-Risk AI Systems*

High-risk AI systems require establishing and implementing a 'risk management system', understood as a "continuous iterative process planned and run throughout the lifecycle" of such systems.[78] Where these systems make use of techniques involving the training of AI models with data, the "training, validation and testing data sets" must be "relevant, sufficiently representative, and to the best extent possible, free of errors and complete given the intended purpose" and must have "the appropriate statistical properties, including, where applicable, as regards the persons or groups of persons about whom the high-risk AI system is intended to be used".[79]

In this regard, the AI Act provides a specific exemption from Article 9 of GDPR, which lays down an exhaustive list of legal bases for processing special personal data categories. Article 10(5) of the AI Act thus permits the processing of such data – "subject to appropriate safeguards for the fundamental rights and freedoms of natural persons' and 'to the extent that it is strictly necessary'- to ensure bias detection and correction".[80]

High-risk AI systems must be accompanied by technical documentation containing at least "the elements set out in Annex IV", which prescribes "a general description of the AI system" and a detailed description of the elements of

76 Article 3(7) AI Act.
77 Article 3(8) AI Act.
78 Article 9(1) and (2) AI Act.
79 Article 10(3) AI Act.
80 Article 10(5) AI Act.

the AI system and the process for its development, "detailed information about the monitoring, functioning and control of the AI system", "a description of the appropriateness of the performance metrics for the specific AI system", "a detailed description of the risk management system", "a description of the relevant changes made by the provider to the system through its lifecycle and a list of harmonised standards applied in full or in part … or detailed description of the solutions adopted to meet the requirements, a copy of the EU declaration of conformity and a detailed description of the system in place to evaluate the AI system performance in the post-market phase". These are to be provided to organisations involved in the assessment of compliance of the AI system with the requirements set out in the legislation.

High-risk AI systems must also "technically allow for the automatic recording of events ('logs') over the system's lifetime"[81] and be "designed and developed in such a way … that natural persons can effectively oversee them during the period in which they are in use".[82] The *raison d'être* of this provision on human oversight is stated in the provision itself: "Human oversight shall aim to prevent or minimise the risks to health, safety or fundamental rights that may emerge when a high-risk AI system is used in accordance with its intended purpose or under the conditions of reasonably foreseeable misuse".[83] It is also reflected in the obligation incumbent on deployers to "assign human oversight to natural persons who have the necessary competence, training and authority, as well as the necessary support"[84] and in the additional specific requirements relating to RBI systems, where no action/decision is to be "taken by the deployer based on the identification resulting from the system unless this has been separately verified and confirmed by at least two natural persons".[85]

Insofar as obligations are concerned, providers must *inter alia* ensure compliance of their systems with the requirements described above, indicate on the system or its packaging/accompanying documentation their name, registered trade name/mark and address at which they may be contacted, have a quality management system in place that ensures compliance with the AI Act and keep logs automatically generated by their systems when under their control.[86] They are bound by rules related to documentation keeping,[87] must

81 Article 12(1) AI Act.
82 Article 14 AI Act.
83 Article 14(2) AI Act.
84 Article 26(2) AI Act.
85 Article 14(5) AI Act.
86 Articles 16(1)(a)-(c) and (e), 17 and 19 AI Act.
87 Article 18 AI Act.

ensure that high-risk AI systems undergo the relevant conformity assessment procedure (referred to in Article 43) prior to their being placed on the market or put into service[88] and must affix the CE marking to such systems to indicate conformity with the Act (per Article 48).[89] This conformity assessment system, discussed in the next section, has been adapted from EU product safety law. Providers who have reason to consider that a high-risk AI system is not in conformity with the AI Act must "immediately take the necessary corrective actions to bring that system into conformity, to withdraw it, to disable it, or to recall it, as appropriate" and inform distributors, deployers, authorised representatives and importers accordingly.[90] When a provider becomes aware that a high-risk system risks an individual's "health, safety, or fundamental rights",[91] they must investigate the cause and inform the competent MSA and, where applicable, the notified body.[92] Providers must cooperate with competent authorities,[93] and where they are established in third countries, they must appoint an authorised representative in the EU by written mandate.[94] Providers must also "establish and document a post-market monitoring system in a manner that is proportionate to the risks of the high-risk AI system"[95] and report any serious incident to the MSA of the Member States where the incident occurred.[96]

Deployers must take "appropriate technical and organisational measures" to ensure they use high-risk AI systems "per the instructions for use".[97] As alluded to above, they must assign human oversight to natural persons[98] and monitor the operation of high-risk AI systems based on the instructions for use.[99] When they have reasons to consider that the use of the instructions may result in the system presenting a risk, they must, without undue delay, inform the provider or distributor and the relevant MSA and suspend the use of the system. They must also inform the provider first, the importer or distributor, and the relevant

88 Article 16(f) AI Act.
89 Article 16(h) AI Act.
90 Article 20(1) AI Act.
91 Article 79(1) AI Act.
92 Article 20(2) AI Act.
93 Article 21 AI Act.
94 Article 22 AI Act.
95 Article 72 AI Act.
96 Article 73 AI Act.
97 Article 26(1) AI Act.
98 Article 26(2) AI Act.
99 Article 26(5) AI Act.

MSA when they have identified a serious incident. If the deployer cannot reach the provider, it must report such an incident to the relevant MSA directly.

Similarly to providers, deployers must keep logs automatically generated by the relevant AI system "to the extent that such logs are under their control".[100] Deployers who are employers must "inform workers' representatives and affected workers that they will be subject to using a high-risk AI system".[101] Deployers of high-risk AI systems for post-remote biometric identification must generally request authorisation from a judicial or administrative authority,[102] and deployers of high-risk systems referred to in Annex III of the Act must inform "natural persons that they are subject to the use of the high-risk AI system".[103] Finally, similarly to providers, deployers must cooperate with the relevant competent authorities.[104]

6.2 *Specific Obligations of Providers of General-Purpose AI Models*

Providers of GPAI models must draw up and keep updated relevant technical documentation, including regarding such models' training and testing process and the results of their evaluation;[105] draw up and make available relevant information and documentation to providers of AI systems who intend to integrate the GPAI model into their systems;[106] put in place a policy to comply with Union law on copyright and related rights;[107] and draw up and make publicly available a sufficiently detailed summary about the content used for training the AI model.[108] Providers of free and open-sourced licence GPAI models are exempt from the first two above-listed obligations; however, providers of GPAI models with systemic risks are not.[109]

Moreover, providers of models with systemic risk are bound by additional obligations to those described above and must also: "perform model evaluation … including conducting and documenting adversarial testing of the model to identify and mitigate systemic risks";[110] "assess and mitigate possible

100 Article 26(6) AI Act.
101 Article 26(7) AI Act.
102 Article 26(10) AI Act.
103 Article 26(11) AI Act
104 Article 26(12) AI Act.
105 Article 53(1)(a) AI Act.
106 Article 53(1)(b) AI Act.
107 Article 53(1)(c) AI Act.
108 Article 53(1)(d) AI Act.
109 Article 53(2) AI Act.
110 Article 55(1)(a) AI Act.

systemic risks at Union level";[111] keep track of, document and report relevant information about serious incidents and possible corrective measures to address them without undue delay to the AI Office and as appropriate national authorities;[112] and ensure an adequate level of cybersecurity protection for the GPAI model with systemic risk and its physical infrastructure.[113]

The Act calls for the drawing up of codes of practice at the Union level relating to GPAI models and corresponding obligations;[114] providers of such models may rely on these codes to demonstrate compliance until harmonised standards are published.[115] Finally, it is also incumbent on providers of GPAI models established in third countries to appoint an authorised representative in the EU.[116]

6.3 *Fundamental Rights Impact Assessment*

The first use of 'impact assessments' concerning data-driven technologies was in the field of privacy and data protection. The terminology 'Privacy Impact Assessment'[117] was later replaced by 'Data Protection Impact Assessment' in the GDPR.[118] The terminology and the intended scope of such impact assessments have been extended to a '*fundamental rights* impact assessment'[119] to consider broader fundamental rights risks of AI systems. The impact assessment criteria would derive from the EU Charter of Fundamental Rights[120] and the European Convention on Human Rights.[121] An 'impact assessment'

111 Article 55(1)(b) AI Act.
112 Article 55(1)(c) AI Act.
113 Article 55(1)(d) AI Act.
114 Article 56 AI Act.
115 Article 55(2) AI Act.
116 Article 54 AI Act.
117 See for example the work of then Information and Privacy Commissioner/Ontario Anne Cavoukian, Privacy Impact Assessment Guidelines for the Ontario Personal Health Information Protection Act (October 2005) <https://www.ipc.on.ca/wp-content/uploads/resources/phipa_pia-e.pdf> accessed 31 May 2023; see also Roger Clarke, 'Privacy impact assessment: Its origins and development' (2009) 25(2) Computer Law & Security Review 123.
118 Article 35 GDPR.
119 Heleen Janssen, Michelle Seng Ah Lee, Jatinder Singh, 'Practical fundamental rights impact assessments' (2022) 30 International Journal of Law and Information Technology 200.
120 Charter of Fundamental Rights and Freedoms of the European Union [2012] OJ C 326/02.
121 Council of Europe Convention for the Protection of Human Rights and Fundamental Freedoms [1953]. On the relationship between these instruments, see Article 52(3) EU Charter: 'In so far as this Charter contains rights which correspond to rights guaranteed

presumes that it is carried out *ex-ante*, i.e. before the AI system is put on the market or released into society. However, *ex-post* or audit-type impact assessments are also essential given the fast-paced development of AI systems, their potential unpredictability, and the consequential significant risks posed to individuals or society.

The AI Act has previously been criticised for lacking a general fundamental rights risk assessment for all AI systems falling within its scope, not just high-risk ones.[122] Moreover, Edwards has criticised the restricted scope of such *ex-ante* assessments, noting, in particular, the lack of systematic concern for impacts on groups, particularly algorithmically constituted groups.[123] What should be legally mandated is a comprehensive *ex-ante* impact assessment, as well as regular *ex-post* audits for algorithmic systems released into society, to identify and mitigate the impact and all potential risks or harms that may result from the deployment of such systems. Moreover, such impact assessment should go beyond the traditional individual human rights approach and consider potential harms to groups and communities.

Today, however, the Act still only requires a fundamental rights impact assessment for high-risk AI systems in specific circumstances. It is only deployers of high-risk systems referred to in Annex III (except those relating to critical infrastructure) that are "bodies governed by public law" or "private entities providing public services", and deployers of high-risk systems intended to be used to evaluate the creditworthiness of natural persons or establish their credit score (except AI systems used to detect financial fraud)[124] and for risk assessment and pricing concerning natural persons in the case of life and health insurance[125] that must assess the impact on fundamental rights that the use of such systems may produce.[126]

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by the Convention for the Protection of Human Rights and Fundamental Freedoms, the meaning and scope of those rights shall be the same as those laid down by the said Convention. This provision shall not prevent Union law providing more extensive protection'.

122 Edwards (n 32).

123 Ibid.

124 Annex III 5(b).

125 Annex III 5(c).

126 Article 27 AI Act.

7 Co-regulation, Standardisation and Certification

High-risk AI systems or GPAI models that follow harmonised standards enjoy a presumption of conformity with the requirements for such systems and models set out in Chapter III, Section 2 or Chapter V, Sections 2 and 3 of the Act.[127]

The Commission can mandate the European Committees for Standardisation ('CEN') and Electrotechnical Standardisation ('CENELEC') to develop harmonised standards.[128] The Commission may also adopt implementing acts establishing common specifications for the relevant requirements where it has requested a standardisation organisation to draft harmonised standards. However, the request has not been accepted, the standards have not been delivered within the deadline, fundamental rights concerns have not been addressed, or the request has not been complied with. No requirement reference has been published in the EU's Official Journal.[129] Systems and models following such specifications will also enjoy the same presumption of conformity described above to the extent that the common specifications cover the relevant requirements or obligations.[130]

Harmonised standards often function as a necessary point of reference for compliance. It is likely, however, that as the AI Act remains vague on how to implement the essential requirements for high-risk AI systems, the responsibility for determining the specifics of these requirements will be delegated to CEN and CENELEC. That standardisation will thus be where the real rule-making occurs. This practice of effectively privately outsourcing complex negotiations has been controversial.[131] For example, Ansari and Mardais argue that the lack of representation from human rights experts or civil society organisations in these bodies raises concerns about their ability to protect fundamental rights. They state that technical standards related to data governance, transparency, security, and human oversight will directly impact fundamental rights and that

127 Article 40 AI Act.

128 Regulation (EU) No 1025/2012 of the European Parliament and of the Council of 25 October 2012 on European standardisation, amending Council Directives 89/686/EEC and 93/15/EEC and Directives 94/9/EC, 94/25/EC, 95/16/EC, 97/23/EC, 98/34/EC, 2004/22/EC, 2007/23/EC, 2009/23/EC and 2009/105/EC of the European Parliament and of the Council and repealing Council Decision 87/95/EEC and Decision No 1673/2006/EC of the European Parliament and of the Council OJ L 316/12. Amended by Directive (EU) 2015/1535 of the European Parliament and of the Council of 9 September 2015 laying down a procedure for the provision of information in the field of technical regulations and of rules on Information Society services (codification) OJ L 241/1.

129 Article 41(1) AI Act.

130 Article 41(3) AI Act.

131 Veale and Borgesius (n 51) 105–106.

the lack of democratic scrutiny or legislative interpretation of these standards may weaken the implementation of the Act.[132]

In addition to ensuring adherence to harmonised standards or common specifications, providers of high-risk AI systems must undertake a conformity assessment.[133] The EDPS and EDPB have called for such assessment to be generally undertaken by third parties. However, the final draft of the Act permits a self-assessment in many cases.

Providers of high-risk AI systems falling within the Annex III category of biometrics that have applied relevant standards or specifications may opt for a self-assessment or an assessment involving a notified body. Such providers must perforce opt for the latter procedure if harmonised standards do not exist if they have not applied or have only applied part of existing standards, or if they have not applied existing specifications.[134] Notified bodies are independent technical organisations to be established under the national law of a Member State[135] and tasked with verifying the conformity of high-risk AI systems.[136] Providers can generally opt for a notified body of their choice unless the high-risk system is intended to be put into service by law enforcement, immigration or asylum authorities or by Union institutions, bodies, offices or agencies. In this latter case, as applicable, the MSA referred to in Article 74(8) or (9) must act as a notified body.[137] Providers of high-risk AI systems falling within the remaining Annex III categories shall conduct a self-assessment without needing third-party involvement,[138] and providers of high-risk AI systems covered by the Union legislation in Section A of Annex I must follow the relevant conformity procedure under those legal acts.[139]

The Act also contains provisions for a 'CE marking of conformity'[140] (or CE certification), an EU declaration of conformity. Digital CE markings shall be used for digitally provided high-risk AI systems.[141]

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132 Mehwish Ansari and Vidushi Marda, 'Opinion. AI Act – leaving oversight to the techies will not protect rights' (*EU Observer*, 5 May 2023) <https://euobserver.com/opinion/156992#:~:text=In%20May%2C%20the%20European%20Parliament,regulate%20the%20use%20of%20AI.> accessed 8 May 2023.

133 Article 43 AI Act.

134 Article 43(1) AI Act.

135 Article 31(1) AI Act.

136 Article 34 AI Act.

137 Article 43(1) AI Act.

138 Article 43(2) AI Act.

139 Article 43(3) AI Act.

140 Article 48 AI Act.

141 Article 48(2) AI Act.

8 Governance and Enforcement

8.1 *Specific Transparency Obligations*

In addition to the obligations under Chapters III, V, and IX described above, the AI Act confers two specific transparency obligations on providers and four on deployers in Chapter IV.

Thus, providers must ensure that AI systems intended to interact with natural persons are designed and developed so that natural persons are informed that they are interacting with an AI system (unless this is obvious from the point of view of a natural person). This obligation does not apply to systems authorised by law to detect, prevent, investigate and prosecute criminal offences, subject to appropriate safeguards for the rights and freedoms of third parties, unless such systems are available for the public to report a criminal offence.[142]

Additionally, providers of AI systems, including GPAI systems, generating synthetic audio, image, video or text content must ensure that the system outputs are marked in a machine-readable format and detectable as artificially generated or manipulated. This obligation is also not applicable to handling criminal offences, nor where such systems perform an assistive function for standard editing or do not substantially alter the input data provided by the deployer or the semantics thereof.[143]

Deployers of biometric categorisation or emotion recognition systems must inform the natural persons exposed to such systems of their operation and process any personal data by the GDPR, even though it remains controversial under data protection law whether facial recognition technology, which processes personal data only transiently falls within the scope of the definition of "personal data" and thus, of the GDPR.[144] This obligation also does not apply to such systems permitted by law to detect, prevent, and investigate criminal offences, subject to appropriate safeguards for the rights and freedoms of third parties.[145]

Deployers of an AI system that generates or manipulates image, audio or video content constituting a deep fake must disclose that the content has been

142 Article 50(1) AI Act.

143 Article 50(2) AI Act.

144 Peter Alexander Earls Davis, 'Facial Detection and Smart Billboards: Analysing the 'Identified' Criterion of Personal Data in the GDPR' (2020) 6(3) European Data Protection Law Review 365; Damian George and Kento Reutimann, 'GDPR Bypass by Design? Transient Processing of Data under the GDPR' (2019) 9 International Data Privacy Law 14; Nadezhda Purtova, 'From knowing by name to targeting: the meaning of identification under the GDPR' (2022) 12(3) International Data Privacy Law 163.

145 Article 50(3) AI Act.

artificially generated or manipulated. Again, this obligation does not apply where the use is authorised by law to detect, prevent, investigate and prosecute criminal offences or where the content is part of a creative, satirical, artistic or fictional work or programme subject to appropriate safeguards for the rights and freedoms of third parties.[146] In such cases, there could be two persons to protect: the one depicted in the deep fake (if it concerns a person) and the audience/recipient of the deep fake. This provision seems focused on the recipient: misplaced beliefs of authenticity may present dangers, particularly fake news and disinformation in media law.

As such, Chapter IV of the Act includes the following final obligation: Deployers of an AI system that generates or manipulates image, audio or video content published to inform the public on matters of public interest shall disclose that the said content has been artificially generated or manipulated. This is also not applicable where use is authorised by law to detect, prevent, investigate or prosecute criminal offences, where the AI-generated content has undergone a process of human review or editorial control and where a natural or a legal person holds editorial responsibility for the publication of the content.[147]

Further specific transparency obligations for providers of GPAI models are also found within the provisions on the obligations of such providers,[148] already referred to above. This is because GPAI models may form the basis for a range of downstream systems, often provided by downstream providers, defined in the Act as a provider of an AI system, including a general-purpose AI system, which integrates an AI model, regardless of whether the AI model is provided by themselves and vertically integrated or provided by another entity based on contractual relations.[149] This necessitates "a good understanding of the models and their capabilities to enable the integration of such models into their products and to fulfil their obligations under [the AI Act] or other regulations".[150]

8.2 *Market Monitoring and Market Surveillance*

Regarding post-marketing controls, the Act provides that each Member State must establish or designate at least one notifying authority and at least one MSA for its purposes as national competent authorities.[151] These authorities are to

146 Article 50(4) AI Act.
147 Article 50(4) AI Act.
148 Article 53(1)(b) AI Act.
149 Article 4(68) AI Act.
150 Recital (101).
151 Article 3(48) and Article 70 (1) AI Act.

exercise their powers independently, impartially and without bias to safeguard the objectivity of their activities and tasks and ensure the application and implementation of such Acts; as long as these principles are observed, such activities and tasks may be performed by one or several designated authorities, per the organisational needs of the Member State.[152]

MSAs should have all enforcement powers under the AI Act and Regulation (EU) 2019/1020.[153] The EDPS will be the competent authority for AI systems put into service or used by Union institutions, agencies, offices and bodies.[154] MSAs will receive information through a chain of notification obligations. For instance, as discussed earlier, deployers who have reason to consider that the use per the instructions of a high-risk AI system may result in that system presenting a risk to the health or safety or fundamental rights of persons must inform (amongst others) the relevant MSA and both providers and deployers of high-risk AI systems are under an obligation to inform MSAs about any serious incidents.[155]

While it is envisaged that investigatory powers will primarily be in the hands of the national authorities, the AI Act also establishes a European Artificial Intelligence Board (AI Board)[156] with specified tasks centrally focused on facilitating the "consistent and effective application" of the Act.[157] During the legislative procedure, the co-rapporteurs of the Act in the EP proposed replacing the AI Board with an EU AI Office, envisaged as an independent body with its legal personality, funding, and staff.[158] The AI Office has since been established by a Commission Decision,[159] with the mission "to develop Union expertise and capabilities in the field of AI and to contribute to the implementation of Union law on AI".[160] At the same time, the AI Board has been retained as an entity to be established by the AI Act.

152 Article 70 AI Act.
153 Recital (156) AI Act. This is also reflected in the definition of an MSA in Art. 3(26) AI Act.
154 Article 70(9) AI Act.
155 Articles 26(5) and 73 AI Act.
156 Article 65 AI Act.
157 Article 66 AI Act.
158 Title VI 'Governance', Chapter 1 'European Artificial Intelligence Office', Articles 56–58, Text adopted by the leading parliamentary Committees of the European Parliament on 11 May 2023 <https://www.europarl.europa.eu/resources/library/media/20230516RES90302/20230516RES90302.pdf> accessed 10 June 2023.
159 Commission Decision of 24.1.2024 establishing the European Artificial Intelligence Office C(2024) 390.
160 Recital (148) AI Act.

The AI Act further establishes a new, central database managed by the Commission to register 'standalone' high-risk AI systems.[161]

> In order to facilitate the work of the Commission and the Member States in the Artificial Intelligence field as well as to increase the transparency towards the public, providers of high-risk AI systems (other than those related to products falling within the scope of relevant existing Union harmonisation legislation) should be required to register themselves and information about their high-risk AI system in a EU database, to be established and managed by the Commission.[162]

The obligation of registration in the EU database has also been extended to deployers of high-risk AI systems listed in Annex III (except systems relating to critical infrastructure) that are public authorities, agencies or bodies.[163]

9 Regulatory Sandboxes

A regulatory sandbox allows innovators to explore and experiment with new and innovative products, services or businesses under a regulator's supervision. It potentially benefits all stakeholders: it allows regulators to understand the technology better, provides innovators with incentives to test their innovations in a controlled environment, and fosters consumer choice in the long run. However, regulatory sandboxes also come with a risk of being misused or abused. To succeed, an appropriate legal framework is needed.[164]

An 'AI regulatory sandbox' is defined in the Act as "a controlled framework set up by a competent authority which offers providers or prospective providers of AI systems the possibility to develop, train, validate and test, where appropriate in real-world conditions, an innovative AI system, under a sandbox plan for a limited time under regulatory supervision".[165]

Member States' national authorities must set up at least one AI regulatory sandbox at the national level and put a framework for governance and

161 Article 71 AI Act.
162 Recital (131) AI Act.
163 Article 49(3) AI Act.
164 Tambiama Madiega with Anne Louise Van De Pol, European Parliament Briefing Artificial Intelligence Act and regulatory sandboxes, June 2022 <https://www.europarl.europa.eu/RegData/etudes/BRIE/2022/733544/EPRS_BRI(2022)733544_EN.pdf> accessed 30 May 2023.
165 Article 3(55) AI Act.

supervision in place.[166] Importantly, participants remain liable under applicable Union and Member States' liability legislation for any damage caused in the course of their participation in an AI regulatory sandbox, although in such cases, provided that the relevant providers observe the plan and terms and conditions for their participation, no administrative fines shall be imposed on them for infringements of the Act.[167] The modalities and conditions for establishing and operating the AI regulatory sandboxes will be adopted through implementing acts.[168] These will include matters such as eligibility criteria, application and selection procedures, participant rights and obligations, and further procedures relating to participation and exit from regulatory sandboxes.

An Open Loop report exploring an earlier version of this provision concluded that it is, in fact, these implementing acts, rather than the provision itself, that could create the necessary conditions for successful regulatory sandboxes. This report warned, however, that Member States should avoid creating conditions that are too favourable for participants, as this could distort the level playing field for AI development in Europe.[169] National competent authorities that have established AI regulatory sandboxes will cooperate and coordinate their activities within the framework of the AI Board and the AI Office.[170]

SMEs, including start-ups, will be provided priority access to the AI regulatory sandboxes and, where appropriate, a dedicated channel for communication to provide advice and respond to queries about the implementation of the Regulation, particularly in AI regulatory sandboxes.[171] It is envisaged that these sandboxes will allow proportionate application of the rules to the SMEs, insofar as permitted under existing legislation, and thus provide a space for experimentation under the new rules and the existing legal framework.[172]

The Act also regulates the processing of personal data in AI regulatory sandboxes for "developing, training and testing certain AI systems", which it

166 Article 57(6) AI Act.

167 Article 57(12) AI Act.

168 Article 58 AI Act.

169 Norberto De Andrade, Laura Galindo and Antonella Parra, 'Artificial Intelligence Act: A Policy Prototyping Experiment. EU AI Regulatory Sandboxes' (Open Loop, April 2023) <https://openloop.org/programs/open-loop-eu-ai-act-program/?utm_source=substack&utm_medium=email> accessed 8 May 2023.

170 Article 57(15) AI Act.

171 Article 62(1)(a) and (c) AI Act.

172 European Commission Impact Assessment of the Regulation on Artificial Intelligence, 21 April 2021, SWD(2021) 84 final, p.71.

considers to be 'further' processing.[173] Such further processing is permitted only when the conditions laid out in Article 59(1)(a) to (j) of the Act are met.

10 Room for National Initiatives in the EU?

In EU law, a 'full harmonisation measure' means that it allows no scope for stricter regulation at the national level. It is unclear whether the AI Act is intended to be such a measure. A discussion of the complex relationship between EU law and national-level laws[174] and the room left for national-level regulation, in particular, if not 'pre-empted' by the AI Act, is too complex to be tackled in the space of this book chapter. Suffice it to say that while the Act is primarily concerned with regulating 'high-risk' AI systems, non-high-risk AI systems are barely regulated but still fall within its scope, thus arguably precluding national legislation on such systems.[175] Having said this, Article 26 concerning obligations of deployers of high-risk AI systems provides that the "obligations [relating to the use of high-risk AI systems and in particular the assignment of human oversight] are without prejudice to other deployer obligations under Union or national law and to the deployer's freedom to organise its resources and activities to implement the human oversight measures indicated by the provider"[176] thus specifically allowing room for national legislation.

11 Conclusion: Regulatory Balance

Regulation is necessary but tricky. It is important to get the regulatory balance right. Too little regulation and important rights and interests may be undermined; too much regulation and innovation, development and investment – and thus, the EU's competitiveness on the global stage – may be stifled. Excessive regulation also tends to help further entrench the market power of the incumbent big players. When discussing regulating AI, an appropriate legal framework should enable investment and innovation while upholding

173 Article 59 AI Act.

174 Discussed in: Stephen Weatherill, *The Fundamental Question of Minimum or Maximum Harmonisation*, in S Garben and I Govaere (eds), The Internal Market 2.0, Oxford: Hart Publishing, 2020, 261–284.

175 Veale and Borgesius (n 51) 110.

176 Article 26(3) AI Act.

and protecting fundamental rights and safety. This also falls within the broader picture of the Digital Single Market in the EU.

Strengths of the AI Act include the risk-based approach, the prohibition of certain AI systems, and the possibility for societal scrutiny via a public database. However, this chapter has also commented on potential weaknesses, such as the role of the standardisation bodies that lack the participation of human rights experts and/or civil society organisations and that are likely to write the real rules against which providers will self-assess.

The AI Act acknowledges the risks to individuals and society posed by AI technologies and seeks to prevent them without stifling innovation. Nevertheless, earlier versions of the Act were criticised for being "generally less encouraging of the development of new AI technologies" and not going far enough to protect fundamental rights.[177] It remains to be seen whether the Act will lead to a balanced model between fundamental rights and technological development or whether Europe's zealousness to regulate this space will mean that innovative businesses will base themselves elsewhere and choose not to offer their services within the EU. Beyond the internal market, the potential global implications of the EU AI Act should also not be ignored, considering the EU's capacity to set *de facto* international standards for AI regulation due to its substantial market size and regulatory influence. In this sense, the EU's influence may extend beyond hard law to a form of soft extraterritoriality—termed the "Brussels effect"—which may encourage non-EU countries and multinational corporations to align their AI practices with EU standards. This and other complex issues will undoubtedly be the subject of several further studies in future.

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177 See Edwards (n 32) and Veale and Borgesius (n 51).

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CHAPTER 7

Can AI Revolutionise How We Do Business: Fact or Fiction?

Tiziana Filletti

Abstract

Across the globe we are experiencing a significant boost in technological developments. Inarguably, AI is the fulcrum of this revolution. As IT continues to grow and develop, a pertinent issue to be addressed is its potential to replace activities traditionally carried out by humans, such as the carrying out of trade and the regulation thereof. Can AI effectively and efficiently replace the business acumen and skilled decision-making of humans in administering and managing business concerns? Commercial partnerships play a vital role in boosting economies. Businesses do not operate in a vacuum but consistently face financial stresses and challenges. It is a fact that AI has made crucial advancements in analysing enormous amounts of data quickly and efficiently. However, is this enough for business purposes? Can the lack of human judgment ever be overcome? Are AI systems sufficiently flexible to adapt to dynamic legal realities? Is the lack of interpersonal engagement a stumbling block? To address these concerns, the recently approved EU AI Act has been explored. The focus here is to examine what has motivated the European Union to pursue this approach and how this legislative effort will influence AI norms globally. These are some of the issues that will be addressed. In short, businesses and regulators need to embrace AI integration – what remains to be seen is the extent to which the two worlds will intertwine.

1 Introduction

Let us imagine someone asking himself or herself the following questions: Is there any reason why I should devote any particular interest towards AI beyond some general information? Is AI a matter of concern to me in any way? I read somewhere that AI may pose risks, but what are these risks? Are they real risks or imaginary ones? Moreover, since I am not the sort of person who likes taking any risks, why should I be bothered?

Let us now consider a few possible scenarios where AI has been set into motion and see whether any element of humans has come into existence.

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Nobody doubts, for example, that human rights and democracy play a vital role in our lives, and we are all aware of their daily challenges. Well, it is important to note that AI can be adapted to undermine human rights by, for example, creating new risks and challenges in matters involving surveillance, manipulation, discrimination, exclusion and even violence. AI can be used not only in a positive way but also in a deliberately negative manner. AI can enable mass and intrusive surveillance by collecting, analysing and sharing vast amounts of personal and sensitive data even without the consent or knowledge of the individuals concerned[1] disseminating false and misleading information or false news. Would you say that these possibilities occurring in our daily lives do not pose risks? If so, how should we proceed with containing these risks?

At the other end of the spectrum one cannot but be overwhelmed positively by learning about developments in the medical field for the benefit of mankind; take one example through AI that would leave no space to harbour any doubt concerning its direct relevance and importance to us. Everyone is interested in reducing human error through AI by using robotic surgery systems that can perform complex procedures with precision and accuracy, reduce human error, and generally improve safety in healthcare. We also realised that AI programs can be made to work endlessly for long hours without breaks, think much better faster than humans, and perform multiple tasks at a time with accurate results. These programs can even handle tedious, repetitive jobs easily with the help of AI Algorithms. During the Covid-19 pandemic, Mater Dei Hospital deployed a new robot which could process 800 coronavirus tests per day and release the result within a few minutes.

Would you rather have a robot defusing a bomb than risk the life of a bomb disposal expert? However, then again, on the negative side of things, what if a man-made drone is programmed to shoot bombs and throw missiles at human beings or destroy hospitals, schools and homes? The list of tasks involving AI is endless and continuously evolving. The few examples I have mentioned are only the tip of the iceberg *vis-à-vis* AI applications.

Ultimately, it all boils down to a question of AI algorithms engineered by humans. For these reasons, the need has long been felt to assess risks involved to the human race and the global environment, to classify and issue rules of conduct and other relevant laws and regulations, including imposing penalties in case of default or violations.

This study will examine how the current AI reality we are experiencing will impact how we do business. There are various evident concerns to mankind,

1 Zuboff, S., & Schwandt, K. (2019). *The age of surveillance capitalism: the fight for a human future at the new frontier of power*. Profile Books.

such as the possibility of job displacement, serious ethical issues relating to bias, privacy, security risks from hacking, and the lack of human-like creativity and empathy. This constant oscillation between good and bad with AI applications is unavoidable. For this reason, international bodies like the EU had to step in at some point to introduce a measure of collective regulatory control across the continent and consider other influential jurisdictions outside Europe.

2 Contextualising the New EU AI Act

Regarding Recital 1, the EU AI Act aims to improve the Internal Market's functionality. It lays down a uniform legal framework for "the development and placing on the market and the use" of AI systems in the Union. This is achieved in accordance with Union values "to promote the uptake of human-centric and trustworthy Artificial Intelligence (AI) while ensuring a high level of protection of health, safety, fundamental rights as enshrined in the Charter".[2] These include the principles of democracy, the rule of law, environmental protection, the protection against the harmful effects of Artificial Intelligence systems in the Union, and support innovation. Its declared aim is that while boosting innovation and employment, the Union will be a leader in the uptake of trustworthy Artificial Intelligence.

The EU AI Act is meant to effectively control and contain the continuous expansion and the rapid recent advances of AI in various areas. The result is not some revolutionary product that surprised everyone but the culmination of a long study, consultation, and exchange process among EU member states. The aim was to draft and agree upon solid legislation to provide a collective and robust course of action throughout the Union.

This landmark legislative achievement places the Union at the forefront in laying down clear and explicit rules for AI usage and, as a result, shaping the EU's digital future. The Act prioritises safety and fundamental rights and promotes innovation and investment in AI technologies. For all this to be rendered possible and doable, AI systems have been divided into four (4) risk-centred categories or groups, namely:

- The unacceptable-risk group;
- The high-risk group;
- The limited-risk group and
- The no-risk group.

2 Charter of Fundamental Rights of the European Union.

The AI Act is only the start of a long regulatory process. It delegates responsibility to the European Commission and a newly established AI office to draft implementation acts and guidelines to address arising future challenges.

3 Why Was the Need to Regulate AI in the EU Felt?

Some form of European legislation on Artificial Intelligence (AI) has been expected since 16 July 2019. On that date, Ursula von der Leyen had pledged that she would have proposed new legislation specifically on AI within one hundred days of her election as President of the European Commission.[3] The road to this goal was long and laborious, but that day was finally here.

The EU AI Act[4] is Europe's first comprehensive AI law. Its full name is *Regulation of the European Parliament and of the Council laying Down Harmonised Rules on Artificial Intelligence* (*Artificial Intelligence Act*) *and Amending Certain Union Legislative Acts*.[5] It aims to address risks to health, safety and fundamental rights.[6] The EU's twenty-seven Member States have unanimously endorsed the AI Act, affirming the political agreement reached in December 2023. Similarly, the Internal Market and Civil Liberties Committees in the European Parliament voted 71–8 (seven abstentions) to approve the result of negotiations with the Members States on the AI Act.[7]

What has motivated the European Union to pursue this approach? Moreover, how will this collective effort influence AI norms globally? Europe's approach faces uncertainty. While it is likely that the AI Act will meaningfully influence global AI norms, several factors may hinder its global diffusion and adoption.[8]

The reason for regulation should be clear. The funds invested in AI development, expansion, and application are substantial. Business enterprises are using increasingly larger datasets to innovate and improve their products. Approximately 182 active AI unicorns are estimated to have a combined enterprise value of $1.3 trillion.[9] Research conducted by Stanford University showed that the private sector investment in Artificial Intelligence in 2021 amounted

3 https://ec.europa.eu/commission/presscorner/detail/en/ip_20_403
4 https://artificialintelligenceact.eu/the-act/
5 2021/0106 (COD).
6 https://ec.europa.eu/commission/presscorner/detail/en/qanda_21_1683
7 https://artificialintelligenceact.eu/the-act/
8 Steven Feldstein (2023) *Evaluating Europe's push to enact AI regulations: how will this influence global norms?, Democratization*, DOI: 10.1080/13510347.2023.2196068.
9 Benaich and Hogarth, "State of AI Report".

to a staggering $93.5 billion. To put this figure into perspective, it doubled the amount invested in 2020. In addition, governments are also increasing the level of investment in AI technologies on account of the level of efficiency and innovation it produces.

4 EU AI Act: a Protection to Society and Companies as Well

The AI Act covers various commercial transactions affecting companies and society. It aims to ensure that AI systems are used responsibly and ethically by any corporation or government in the EU, regardless of where these systems are developed or deployed. Its impact is so significant that even businesses set up and established beyond EU borders must follow the Act's rules if they want to operate in Europe.

Therefore, The AI Act should be viewed as a clear signal for businesses, alerting them to ensure their AI systems are safe, clean and respectful of their users.[10] Of course, the AI Act is imperfect, and even companies must grapple with what compliance requires. It is, however, a regulation with teeth and is part of a growing movement to protect society from the worst of what emerging technologies like AI have to offer.[11] Companies can also use it to safeguard their products and services, even if they do not want such assistance. Companies must continue to maximise innovation in these emerging technologies. At the same time, all companies must ensure regulatory compliance and protect their companies from the loss of trust that comes with ethical breaches or corporate misgovernance, whether they are in the EU or elsewhere.

5 The Brussels Effect – a Europe for the Digital Age

Following the Digital Market and Digital Services Act in 2022, the AI Act is the last technology-related legislation passed under the 2019–2024 European Parliament and Commission as part of their mission to create a "Europe fit for the Digital Age".[12] It concludes a mandate characterised by trying to

10 Kostiantyn Ponomarov, *The EU AI Act overview: what's coming for business, Legal Nodes*, March 20, 2024.

11 Harvard Business Review, Reid Blackman and Ingrid Vasiliu-Feltes, the EU's AI act and how companies can achieve compliance, February 22, 2024.

12 Alex Krasodomski, Marjorie Buchser, "*The EU's new AI Act could have global impact*", 13 March 2024, Chatham House.

contemporaneously augment scrutiny of tech whilst promoting digital innovation regulation.

The pivotal question will be whether the so-called Brussels effects will be felt in AI and whether the new regulation will have global consequences for the development of this technology. There is an important precedent of EU regulation impacting outside EU borders. The 2016 General Data Protection Regulation (GDPR) gradually led to global changes as platforms rolled out compliance. There remains debate as to how significant its impact on privacy has been as internet users instead drowned in a wave of opt-in consent popups. However, the impact of the European Regulations on the world is unquestionable. Within a couple of years, giants like META and Microsoft had updated their services and privacy standards. The AI Act is a clear statement that Europe believes it can both regulate AI and, at the same time, remain open for business.[13]

6 The Competition Policy of AI Technologies and AI Start-Ups

The competition policy implications of AI technologies are not clear at present.[14] The development and training of frontier models can cost millions of euro and are often beyond the reach of AI start-ups. Start-ups are more innovative and closer to the AI technology frontier. However, they require close collaboration agreements with large tech firms that make expensive computing infrastructure and data available for access to the model. The agreement between the French AI start-up Mistral and Microsoft is a case in point. France, for example, has repeatedly argued that certain provisions could stifle innovation and hinder European AI start-ups like France's Mistral AI, LightON or Hugging Face, which seek to compete with American companies such as Open AI or Google.[15] France agreed to consent to finalise the Act and join the other member states that had done so already. France's general concern was that the Act risked hampering European tech companies compared to rivals in the US, UK and China, setting the stage for a new battle over regulation of the emerging technology. In the words of French President Emanuel Macron:[16]

13 Alex Krasodomski, Marjorie Buchser, "*The EU's new AI Act could have global impact*", 13 March 2024, Chatham House.

14 Bruegel, author Bertin Martens, 7 March 2024.

15 LeMonde, France keeps up pressure on EU's AI Act despite mounting criticism, Alexandre Piquard, 27 January 2024.

16 Address at Toulouse on Financial Times, Artificial Intelligence, December 11, 2023.

> We can decide to regulate much faster and much stronger than other major competitors. But we will regulate things that will no longer produce or invent. This is never a good idea.

To what extent smaller AI models that are sufficiently performant for a wide range of tasks can compete with larger firms and models remains an open question.

The EU is keen, however, to show that it can innovate and regulate.[17] The EU AI Act sends a clear message that Europe understands that it must regulate AI whilst still promoting business. According to Politico, the EU has seen the need to soften those critics who feared that the new rules could hamper Europe's competitive position against the US, China and others.[18] EU executives are in the process of talking up their efforts to give European start-ups what they need to keep up in the global AI race, such as personnel, money, data and computing powers. Referring to the corporate front-runners in the global AI race, Commission chief von der Leyen[19] has recently announced a new plan to provide start-ups and SMEs access to European supercomputers, similar to what Microsoft is doing for Chat-GPT by running it on its computers. She also singled out an area where Europe should lead the pack: Industrial AI. In this respect, the EU Commission has already put the groundwork in place to improve the sharing of machine-generated data, which could, in turn, prove to be pivotal for automation and the industries' use of AI.

One man's meat is another man's poison, the saying goes. Well, some analysts decry the Act as one "*littered with concessions to industry lobbying over protecting people and human rights*" and "*exemptions for the most dangerous uses of AI by law enforcement and migration authorities*", and that is "*full of loopholes*".[20] It will lead, for example, to the use of digital technologies in new and harmful ways to show up as "Fortress Europe" and to limit the arrival of vulnerable people seeking safety. Civil rights groups view the Act as siding with the interests of businesses, police forces, and governments. Critics, in general, were upset that there was no total ban on face recognition and other mass surveillance technology. They claim the EU is under immense pressure to prevent its companies from being eclipsed in the AI race. This contrasts sharply with criticism

17 Politico, To shush AI critics the EU fine-tunes innovation pitch, Glan Volpicelli reporting, March 2024.

18 Politico, To shush AI critics the EU fine-tunes innovation pitch, Glan Volpicelli reporting, March 2024.

19 https://ec.europa.eu/commission/presscorner/detail/en/ip_24_383

20 Landmark Artificial Intelligence Act in EU slammed as rights "failure" – Jessica Corbett, March 23, 2024, commondreams.org.

from business groups who said it would stifle innovation with its restriction and time-consuming and costly rules. Some even suggested that these AI regulations could lead to an exodus of European AI companies and talent-seeking growth elsewhere.[21] So, you have this tug-of-war between critics decrying loopholes to the detriment of human rights and civil protection, as well as overregulation and stifling effects upon innovation by the business lobby.

7 The Act's Implications for Companies

According to an insightful study published in the *Harvard Business Review*,[22] it is useful for companies to look at AI through the lens of business capabilities rather than technologies. Of course, this is not the same as saying that these capabilities are not implemented through the available appropriative cognitive technologies and applications. In a general way, it was noted that AI could support three important business needs:

i. Automating business processes;
ii. Gaining insight through data analysis and
iii. Engaging with customers and employees.

Some critics have left little time to voice their concerns regarding the Act's implications for companies across several areas and sectors. They have raised questions about how the various provisions could potentially compromise the overall efficiency of these models, leading to an increase in operational costs that could render some companies financially inaccessible. As such, the criticism is not meant to detract from the obvious positive aspects represented by this new EU Act in seeking to address transparently and tangibly the many challenges arising from AI but to point out from the outset that the principle of one-size-fits-all can be both unfair and prejudicial to certain sectors, particularly in the case of new small and/or limited businesses. Critics claim that the AIA is "overly restrictive" in its approach. It limits the potential benefits of AI. Its risk classifications are too stringent, and the compliance requirements could be "overly burdensome" for smaller AI developers.

The definition of AI in the Act was amended. However, despite these amendments, one main concern is that the current definition is too far-reaching and continues to catch within its remit basic software systems. Some critics

21 Cain Burdeau, *EU moves to regulate AI, but critics decry loopholes as Big Tech warns of over-regulation*, December 11, 2023, Courthouse News Service.

22 AI for the real world, T.H. Davenport and R. Ronanki, The Magazine, January–February 2018.

regulating such basic software systems, which do not evidently pose a significant risk, could stultify future innovation. Furthermore, it may result in the undesirable effect of legal uncertainty about what should be considered AI.[23]

The AI Act now has more than fifty vague definitions.[24] Some critics argue that the Act, as it is coming into existence, arguably constitutes "failure by design". Rutkowski,[25] to prove his point, refers to recital six (6), which states that "the notion of the AI system in this Regulation should be clear defined and closely aligned with the work of international organisation working on AI to ensure legal certainty, harmonisation and wide acceptance …". This is easier said than done. Another recital – recital ten – is no less worthy of praise but extremely vague by way of application from a jurisdictional aspect "this Regulation should not apply to public authorities of a third country and international organisation when acting in the framework of international agreements conclude at national or European level already apply or are relevant AI systems today" and then the text goes on "to cite its own law combined with vague references to "UN Human Rights treaties … Council of Europe Conventions and national law". In short, the vagueness begins with the basic definition of an AI system and extends to almost every entity and matter in the Act.

For the above reasons, it is argued that the AI Act runs the risk of being a "failure by design" since "simply throwing every legal, regulatory mechanism upon the wall to see if it somehow sticks, notwithstanding so many omissions and infirmities, to somehow govern the AI universe will not work".[26] It is conceded that there is one exception to this harsh assessment, namely, facilitating harmed parties to institute civil actions against wrongdoers – a course of action that should work and deserves support and praise.

8 Companies, Company Employees and AI-Anxiety

Before embarking upon a more detailed review of the Act concerning its possible impact on Maltese company law, I would like to briefly dwell upon an important ethical point concerning companies and their employees considering developing AI strategies within their structure and productivity goals.

23 The EU AI Act: concerns and criticism – Clifford Chance AI Talking Tech – Tamlin Higgins, Robin Jackson, Prepijn Koiter – 6 April 2023.

24 Circle ID, Anthony Rutkowksi, The EU AI Act: A critical assessment, June 28, 2023.

25 Ibid.

26 Ibid.

Ever since the onset of the Industrial Revolution in the middle of the nineteenth century, certain categories of workers, especially those that were lower in terms of skills, felt that they might eventually lose their jobs and be replaced by machinery. They failed to realise then that the machines would increase production and create other new opportunities. However, this fear of becoming redundant never really disappeared entirely. The technological advancement that followed over the years gave rise to other forms of fear and concern, and eventually, the term technophobia came into being and is still thriving.

The fear of computers, robots and other comparable technologies led to this new phobia. Moreover, now, alongside the remarkable advancements of AI in various spheres, yet another or rather form of fear has emerged. When the fear or rather anxiety is specifically related to a new work has recently been created to describe this particular mental state, namely "AI-anxiety". Some people feel anxious not just about what exists but also about what is unknown to them. A state of "AI anxiety" stems from uncertainty about AI's potential, for example, to create fake videos or spread disinformation that polarises people. Another form of AI-produced content can provoke negative emotional reactions among its viewers. These types of apprehension, sometimes fuelled by science-fiction narratives, come from concerns about existential risks like personal health issues, job displacement, ethical matters and the unintended or even intended consequences of humankind's determination to keep pushing more and more.

If we were to piece together the various elements that may cause anxiety within the ethos business companies, some points of interest will come to the fore. Employees may feel uneasy as AI evolves and more companies develop AI strategies. Typical apprehensions may range from AI replacing jobs – something already mentioned – to losing out on promotions simply for not knowing how to use the new technology. So evidently, in such a case, learning how to use AI responsibly can be the right way to lower anxiety and feel in control.

There is no doubt that deep down, workers are anxious about AI – and that anxiety is directly linked to a lack of communication from the company's management as companies move ahead with their digital transformation. Would it be ethical to leave their employees in the dark? Experts believe that companies owe a certain measure of transparency to their employees. Beyond mere words, some experts believe that companies have an ethical obligation to take action to equip their employees with new skills to meet the coming AI challenges.

Some experts[27] speak about how the manipulation of social media platforms might create population stress, anxiety, depression and feelings of

27 Michael Muller, *AI Experts Predict the Best and Worst Challenges in Digital Life by 2025*, Pew Research Centre Report, 21 June 2023.

isolation. Others refer to problems that have been linked to generative AI systems. These systems can produce erroneous and unexplained facts and can be used to foment misinformation or dupe unwary followers. Experts are also anxious about the seemingly unstoppable spending and scope of digital tech that they fear could enable blanket surveillance of large populations, which could corrupt and destroy the information environment or undermine democratic systems with deep fakes, misinformation and harassment.

All the above considerations may make one feel more concerned than excited about future technological change or, perhaps, equally concerned and excited. Expert opinions on AI technology and its potential are wide and varied. As one researcher aptly put it:

> We will learn new ways in which humans and AIs can collaborate. Humans will remain the centre of the situation. That does not mean they will always be in control, but they will always control when and how they delegate selected activities or one more AI".[28]

In the words of H. James Wilson,[29] "The No. 1 source of worker anxiety is around ensuring the relevance of their skills". It remains to be seen if companies will act ethically to provide transparency – and restrain – to employees skittish about AI. In the meantime, as AI reshapes the business ecosystem, one thing emerges: right or wrong, it makes good business sense and, therefore, is a step in the right direction to include employees in the AI evolutionary process.

9 How Does the New AI Act Impact Maltese Companies, if at All?

To begin with, everybody knows or should know that ignorance of the law is no excuse. This effectively means that the law is there to be applied and enforced upon everyone regardless of whether one is aware of such a law. It therefore follows that the non-compliance with prohibited AI violations mentioned in the Act would, on conviction, lead to a fine. The same applies in other cases of non-compliance, such as supplying incorrect, incomplete or misleading information to notified bodies and national competent authorities in response to a request. Consequently, for example, a company setting up an AI system for an

28 Michael Muller, *AI Experts Predict the Best and Worst Challenges in Digital Life by 2025*, Pew Research Centre Report, 21 June 2023.

29 H. James Wilson, Human and Machine: Reimagining Work in the Age of AI. Boston, MA, Harvard Business Review, 2018.

EU market must ensure compliance with the EU AI Act.[30] Therefore, in such a scenario, an AI risk management system must be on board to fulfil transparency obligations pursuant to the Act. The specific obligations incumbent on a company depend upon the risk level an AI system poses to people's safety, security or fundamental rights along the AI value chain. The most significant transparent reporting requirements will be for those AI systems classified as "high risk" and general purpose AI systems providers purporting to be high-impact or less posing "systemic risks". These legal requirements are bound to generate high compliance costs, especially for SMEs and start-ups that might find the EU regulatory environment too expensive and risky to adhere to. It would be up to the European Commission and the newly established office to monitor future developments and intervene, if necessary, with additional guidelines and corrective measures.

10 The Strategy and Vision of AI in Malta

Going through the official reports, various newspaper articles and other written contributions on Artificial Intelligence, strategies and projections regarding Malta, one might get the impression that, in general, the tone used tends to be enhanced with too much hype and optimistic jargon in terms of potential achievements that one would normally expect, also considering that, overall, AI development and use in Malta is still relatively modest rather than ground-breaking.

By contrast, when mentioning specific examples of AI applications, the tone becomes more down-to-earth and realistic. A case in point concerns introducing and applying software AI within the inland revenue department for local tax collection practices. The Malta AI strategy lacks financial provisions or estimations for its overall implementation.[31]

During a recent event held by the Bank of Valletta,[32] it was noted that, despite advances made, Europe finds itself approximately 1.5 years behind North America in embracing innovations brought in through AI applications. The need was felt for banks to identify strategic entry points across various functions to realise transformative changes through AI. AI introduces important shifts towards greater automation and efficiency. These AI developments encompass sophisticated applications in risk management, fraud prevention

30 Credo, AI, Getting ready for the EU AI Act with Credo AI, 2024.

31 The European Commission's Report on Malta's AI strategy://ai-watch.ec.europe.eu

32 Times of Malta, 9 April 2024 "BoV talks Artificial Intelligence in the banking world".

and tailored customer service. This shift requires broad upskilling initiatives across different teams within the organisation. Meanwhile, for banks to operate at scale successfully, it will be necessary to create interlinkages between engineering expertise and leveraging AI tools. According to the bank's chief strategy, transformation and data officer, Mr Ivo Camilleri, such an investment in change through AI application will translate "into better risk management and enhances customer experience".

11 Malta: Long-Term Vision

The strategy and vision for AI in Malta 2030[33] were developed by the Malta AI task force commissioned by the government of Malta. It aims to prioritise Malta as a leader in the AI field, gaining a strategic competitive advantage globally. The overall vision involves both the public and the private sector. The strategic pillar concerning the private sector outlines initiatives to promote awareness and enable companies of all sizes to use, develop and integrate AI applications within their organizations. Support measures include access to technological expertise, provision of toolkits, and financial assistance.

The strategy is set up on three strategic pillars, namely:[34]

i. The investments, start-ups and innovation pillar;
ii. The public section adoption pillar and
iii. The private sector adoption pillar.

Three strategic enablers, in turn, support each pillar:

i. Education and workforce;
ii. Ethical and legal considerations; and
iii. Ecosystem infrastructure.

Following a review of its national AI strategy, the Malta Digital Innovation Authority (MDIA) invited all stakeholders to submit their views and comments to present a realigned strategy in 2024. Earlier, Malta hosted the EU Med 9 Meeting, focussing on the transformative potential of AI. The meeting stressed the need for collaboration, knowledge and exchange, and the development of a strong AI infrastructure.

33 https://www.mdia.gov.mt/malta-ai-strategy/#:~:text='Strategy%20and%20Vision%20for%20Artificial,contributions%20to%20the%20global%20economy

34 https://digital-skills-jobs.europa.eu/en/actions/national-initiatives/national-strategies/malta-strategy-and-vision-artificial-intelligence

12 AI and Tax Collection in Malta

At the beginning of March 2023, the Ministry of Finance in Malta announced that the government was introducing Artificial Intelligence software in order to assist the local tax authorities in processing tax returns quicker as well as to alert the tax administration authorities if, for example, an individual's wealth assets personal portfolio significantly jars with his or her tax declaration. During the launch of this event to announce a comprehensive tax strategy for tax and customs administration, the finance minister explained that the new software, costing around three million euro, was already in use in other countries like the United Kingdom, New Zealand, the Netherlands, Ireland and Canada. The Minister explained that the software will help alert authorities when a person or business's declared income foes do not tally with their accustomed wealth. It will make detecting tax evasion and acting on it easier and faster. From our point of view, its relevance stems from the fact that it is a statistical analysis system (SAS) that uses Artificial Intelligence to draw data from different registries to assess the individual's liquid and illiquid assets, like property, land, vehicles and boats and compare them to their declared income in a bid to help the tax department keep tabs on income and tax dues. The software will not have access to people's transactions. However, the tax department will retain the legal right to ask banks for that information if it launches an investigation into a company.[35] To allay taxpayers' fears, the finance minister assured his listeners that the government "… will not turn into Big Brother".

13 AI Technology and Future Trends

The advent of Artificial Intelligence has brought change to the world we live in. Many innovations in the field of AI are rapidly shaping the future of humanity across nearly every industry. AI is already a major driver of emerging technologies like big data.[36] Robotic and generative AI is already the norm, from ChatGPT to facial recognition, self-driving cars and virtual assistants such as Alexa and Siri. In addition, machine-learning algorithms trained on massive datasets provide a powerful tool for advancing scientific research.[37] AI is also creating new opportunities across various industries and sectors. Public and

35 M.L. Zammit "*We won't turn into big brother: AI detection of tax cheats*", Times of Malta, 15 May 2023.

36 Peter van der Made, *The Future of Artificial Intelligence*, Forbes, 10 April 2023.

37 VC San Diego Today, "*The Future of AI is Now*", 2 November 2023.

private companies quickly realise that given the correct guidance and structure, AI can impact every aspect of human life. Therefore, Companies would do well in seeking to develop AI strategies to outline areas where AI would be most effective. AI can identify patterns, detect trends, and accurately predict future outcomes. In this way, one could anticipate customer demand, optimize the business' supply chain and make informed decisions in real-time. By leveraging predictive analytics, businesses can reduce costs, improve operation efficiency and enhance overall decision-making. Only time will tell what the future has in store for machine learning and those behind the implementation of Artificial Intelligence.[38]

AI enables companies to offer users and their clients a personalised, tailor-made experience to suit their needs. By analysing user behaviour and preferences, AI technology helps e-commerce platforms recommend products most likely to appeal to specific users based on their search history and previous purchases. This level of personalization not only enhances user experience but also boosts customer satisfaction and loyalty.[39] In short, AI-powered personalization is a crucial aspect of modern technology and an unprecedented boon to business companies and their clientele.

With the constant advancement in technology, we can easily look forward to even greater breakthroughs in the future. We expect to witness more highly advanced technology in different industries in the years ahead. We have seen that AI can optimise logistics and supply chains, making them more efficient and cost-effective. AI may seem surreal for its incredible ability to automate repetitive and time-consuming tasks. The future of AI looks bright. With the right approach, humanity can benefit from the evident advancements in AI technology while tackling challenges and curbing unacceptable uses in its deployment.

14 Conclusions

In conclusion, the EU AI Act puts forward a European set of rules regulating AI – the first of its kind by a major regulator anywhere. Its implementation will ensure that AI rules do not overburden companies trying to innovate and

38 Kristie Wright, *Latest developments of AI: 10 AI trends to follow*, 21 March 2024.

39 Mario Mirabelle, *The Future of Artificial Intelligence: Predictions and Trends*, 11 September 2023, Forbes.

compete in a thriving, highly dynamic market.[40] EU countries still have enough room to influence how the AI law will be implemented. For a start, the European Commission still needs to draft several secondary pieces of legislation.

During a plenary session held on 19 April 2024, a "*Corrigendum*" was made to the position of the European Parliament adopted at a first reading on 13 March 2024 with a view to the adoption of Regulation (EU) 2024. The Act is fully applicable twenty-four months after entry into force, but some parts will be applicable sooner:

i. The bar of AI systems posing unacceptable risks will apply six months after the entry into force;
ii. Codes of practice will apply nine months after entry into force;
iii. Rules on general-purpose AI systems that must comply with transparency and requirements will apply twelve months after they enter into force;
iv. High-risk systems will have more time to comply with the requirement as the obligations concerning them will become applicable thirty-six months after the entry into force.[41]

By way of conclusion, to redress this fluctuating system, it is pertinent to consider the assessment carried out by Brooks,[42]

> … we cannot access the incredible power of AI to do good without simultaneously creating the ability to do wrong. These two will always go hand in hand. A race to create utopia with AI also opens the door to dystopian scenarios … We have much to gain from using AI wisely and much to lose from using it foolishly or recklessly.

Therefore, businesses in general must look at the Act as a compliance necessity and through the broader lens of the reinvention agenda precisely "because every role in every enterprise has the potential to be reinvented in the AI revolution".[43] The choice, at least for now, is still in our hands. Before it is too late, let us avoid being outsmarted by our own doing!

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40 Foo Yun Chee, Europe within reach of landmark AI rules after nod from EU countries, February 2, 2024, Reuters.

41 EU AI Act: first Regulation on Artificial Intelligence, published June 8, 2023, Topics, European Parliament.

42 https://www.psychologytoday.com/intl/blog/tech-happy-life/202310/the-ai-domino-effect-how-ai-will-soon-outsmart-us-all

43 Jean-Marc Ollagnier, *AI Meets Regulation – Driving Innovation with the EU Act*, March 25, 2024, Forbes.

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CHAPTER 8

Boosting Digital Finance and the Digital Single Market?

An Overview of the Rules on the Offering of Crypto-Assets According to the Markets in Crypto-Assets Regulation

Ioannis Revolidis

Abstract

The European Union is the first regional bloc to implement a comprehensive legal framework for the complex and constantly evolving cryptocurrency industry. The author proposes to dissect the implications of the Markets in Crypto-assets Regulation (Regulation (EU) 2023/1114 of the European Parliament and of the Council of 31 May 2023 on markets in crypto-assets and amending Regulations (EU) No 1093/2010 and (EU) No 1095/2010 and Directives 2013/36/EU and (EU) 2019/1937 - MiCA), with a specific focus on the rules about the issuance of crypto-assets. This chapter critically examines how the MiCA Regulation categorises various crypto-assets and delineates the regulatory requirements for their issuance and circulation. MiCA's role in establishing a general framework to mitigate the inherent risks of the crypto industry is assessed, alongside a discussion of the Regulation's potential gaps and ambiguities.

1 Introduction

Over the past fifteen years, crypto-assets have garnered significant attention, frequently becoming the focal point of discussions across multiple spheres, including public discourse, investor forums, and academic circles. The concept of digital assets has roots that extend back to the history of emerging technologies. Indeed, the inception of digital assets can be traced to the 1980s,[1] marking the beginning of a technological revolution that sought to reimagine

1 Many of the ideas that would later spark the digital asset revolution can be traced to the work of David Chaum in such papers as David Chaum, 'Blind Signatures for Untraceable Payments' in David Chaum, Ronald L Rivest, and Alan T Sherman (eds), Advances in Cryptology (Springer, Boston, MA 1983) 199, David Chaum, 'Security without identification: transaction systems to make big brother obsolete' (1985) 28(10) Communications of the ACM 1030.

 | DOI:10.1163/9789004712119_010

traditional financial paradigms. This early experimentation laid the groundwork for what would eventually evolve into today's complex landscape of cryptocurrencies and blockchain technology.[2]

Despite the significant involvement of consumers and investors in digital markets over an extended period, a profound and cataclysmic economic event was required to catalyse a renewed interest in digital currencies and digital assets more broadly. The resurgence of attention towards these digital solutions can be traced back to the 2008 financial crisis when the conventional financial system experienced a severe loss of credibility.[3] The Bitcoin white paper proposed an alternative to the traditional financial system, advocating using cryptographic technologies to secure peer-to-peer digital transactions.[4] The crypto universe was designed to operate independently of established financial intermediaries, including banks and even sovereign governments, which were seen as contributors to the financial instability of the time. The essence of this proposition was to create a financial ecosystem that was more transparent, decentralised, and resilient, qualities that were sorely missing in the traditional frameworks of finance during the economic downturn of 2008.

Consequently, crypto-assets have emerged as a pivotal component of an expansive technological evolution that aims to overcome the technological hurdles that hampered the development of digital assets in the past.[5]

This technological evolution has yielded tangible results in certain ways, as crypto-assets have seemingly withstood the test of time and now appear as a relatively permanent element within the broader digital landscape.[6] Moreover, crypto-assets might introduce significant opportunities in the financial sector

2 For a historic overview of the developments that gradually led to the creation of crypto-assets see Aljosha Judmayer, Nicholas Stifter, Katharina Krombholz, and Edgar Weippl, 'Blocks and Chains: Introduction to Bitcoin, Cryptocurrencies, and Their Consensus Mechanisms' (Springer 2017).

3 For the complex reasons that led to the loss of trust and confidence in traditional economic institutions during the 2008 financial meltdown see Fran Tonkiss, 'Trust, Confidence and Economic Crisis' (2009) 44 Intereconomics 196.

4 Satoshi Nakamoto, 'Bitcoin: A Peer-to-Peer Electronic Cash System' (2008) <https://bitcoin.org/bitcoin.pdf> accessed 23 April 2024.

5 For this double character of the development of digital assets in the sense that it is partially a reaction to the socio-economic failures of the 2008 economic collapse and partially a technological evolution of previous efforts see Tim Marple, 'Bigger than Bitcoin: A Theoretical Typology and Research Agenda for Digital Currencies' (2021) 23 Business and Politics 439.

6 Tina van der Linden and Tina Shirazi, 'Markets in Crypto-Assets Regulation: Does It Provide Legal Certainty and Increase Adoption of Crypto-Assets?' (2023) 9 Financial Innovation 22, who conclude that crypto-assets are "here to stay".

and benefit the development of the common market within the EU.[7] They may, for example, facilitate cost-effective and rapid payment solutions, which are especially advantageous for cross-border and international transactions. They also have the potential to open up new funding opportunities for small and medium-sized enterprises (SMEs) and enhance the efficiency of capital markets.[8] Beyond finance, crypto-assets may enable more streamlined transactions across various industries, including mobility, energy, and manufacturing. Finally, crypto-assets promise to redefine our interactions with other digital assets, such as music, videos, movies, and books. They aim to foster a stronger peer-to-peer ethos in our engagement with these media, thereby reducing the overwhelming influence wielded by powerful centralised platforms.[9]

Nonetheless, it is important to acknowledge that crypto-assets are not devoid of risks, as with nearly all technological innovations. The past few years have provided several characteristic examples highlighting the essential principle that no innovation should operate without supervision and robust guarantees to ensure the resilience, integrity, and safety of the outcomes it produces.[10]

Against this complex and rapidly evolving backdrop, the European legislator felt compelled to intervene and establish a legal framework designed to bring rationality and structure to the operations of crypto markets. As articulated in the Digital Finance Strategy of 2020, the rationale behind such legislative intervention was twofold: firstly, to harness the benefits of financial innovation underpinned by blockchain and Distributed Ledger Technology (DLT), and secondly, to safeguard the integrity of the common market along with upholding the overarching European values of responsible innovation.[11] This was to

7 For the possible opportunities presented by the adoption of crypto-assets see European Commission, 'Digital Finance Strategy for the EU' (COM(2020) 591 final, 24 September 2020) <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52020DC0591> accessed 23 April 2024, 10.

8 See in more detail Randy Priem, 'Distributed Ledger Technology for Securities Clearing and Settlement: Benefits, Risks, and Regulatory Implications' (2020) 6 Financial Innovation 11.

9 Matt Fortnow and QuHarrison Terry, The NFT Handbook: How to Create, Sell and Buy Non-Fungible Tokens (1st edn, Wiley 2021), 47–57.

10 High profile incidents such as the crash of the Terra/Luna algorithmic stablecoin or the collapse of the FTX exchange serve as stark reminders of the different vulnerabilities of the crypto-asset ecosystem. For an assessment of the most recent crypto crashes and panics see Roberto Moro-Visconti and Andrea Cesaretti, 'The Cryptocurrency Crash of 2022: Which Lessons for the Future?' (Palgrave Macmillan, Cham 2023), 395–410.

11 European Commission, 'Digital Finance Strategy for the EU' (COM(2020) 591 final, 24 September 2020) <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52020DC0591> accessed 23 April 2024, 4.

be achieved through effective Regulation of risks and a robust mechanism for consumer and investor protection.[12]

This legislative endeavour reached a significant milestone by adopting the Markets in Crypto-assets Regulation (from now on referred to as MiCA) in May 2023.[13] It is imperative at this juncture to highlight that the primary objective of the MiCA Regulation is not the Regulation of assets per se. Instead, it aims to meticulously regulate the activities of certain pivotal stakeholders who play a central role within the crypto markets. Specifically, the MiCA Regulation targets the issuers of crypto-assets and the providers of crypto-asset services.[14]

The primary purpose of this paper is to present an overview of the key regulatory decisions made by the European legislator within the framework of MiCA with a specific focus on the rules regarding the offering of crypto-assets. It is important to note that this paper does not endeavour to deliver a detailed analysis of each provision within the MiCA Regulation. Instead, it aims to elucidate the underlying philosophy, the regulatory techniques employed, and the principal pillars that support the EU's ambitious efforts to remain at the forefront of market innovation.

2 The MiCA Regulation Uncovered: the Scope of the Application

As regards its scope of application, the MiCA Regulation classifies crypto-assets into three distinct categories. This fundamental regulatory framework is

12 The European approach to the regulation of crypto-assets could be compared and contrasted to the approach of other important jurisdictions such as the USA and China. For instance, both the USA and the EU tolerate the existence of crypto-assets and do not seek to ban access to crypto-assets and crypto services. However, unlike in the EU, the US legislator has, for the time being, avoided introducing a tailored regulatory regime specifically for crypto-assets. China, on the other hand, decided to enhance governmental control over currency and asset markets, and decided to prohibit interactions between traditional financial institutions and the crypto universe. For an overview of the regulatory approach of the USA on crypto-assets see Scott D. Hughes, 'Cryptocurrency Regulations and Enforcement in the U.S'. (2017) 45 W St U L Rev 1. For a comparison between the EU, US and Chinese approach to crypto-asset regulation see Eugenia Siracusa and Giovanni Zaccaroni, 'Regulation of crypto-assets in the EU and in the Rest of the World: A Pluri-Focal Approach' (2021) 3/4 Il Diritto Dell'unione Europea 583, while for a more detailed comparison between Chinese and the US approaches see Rain Xie, 'Why China Had to Ban Cryptocurrency but the U.S. Did Not: A Comparative Analysis of Regulations on Crypto-Markets between the U.S. and China' (2019) 18 Wash U Global Stud L Rev 457.

13 European Parliament and Council of the European Union Regulation (EU) 2023/1114 of 31 May 2023 on Markets in Crypto-Assets, and Amending Regulations (EU) No 1093/2010 and (EU) No 1095/2010 and Directives 2013/36/EU and (EU) 2019/1937 [2023] OJ L 150/40.

14 See Recital 20 of the MiCA Regulation.

delineated in Titles II, III, and IV of its main body. This classification scheme is further affirmed by an examination of Recital 18, which confirms that MiCA adopts a tripartite model for categorising crypto assets. The primary criterion for distinguishing between these categories is whether and how the crypto-asset seeks to stabilise its value by referencing another asset.

In that sense, MiCA introduces the following categories of crypto-assets: a) e-money tokens,[15] b) asset-referenced tokens[16] and c) all other types of crypto-assets that are neither asset-referenced tokens nor e-money tokens.[17] This classification scheme carries significant legal implications, as MiCA tailors the regulatory framework for issuing a crypto-asset based on this categorisation. E-money tokens are regulated under Title IV, asset-referenced tokens under Title III, and all other types of crypto-assets that do not qualify as Title II governs asset-referenced or e-money tokens. This structured approach ensures that each crypto-asset category is subject to a regulatory regime that reflects its specific characteristics and risks.

To a certain extent, one can still discern some overlap with previous classification efforts within the new regulatory framework established by MiCA.[18] However, MiCA decisively concentrates on payment assets and, more precisely, stablecoins.

Furthermore, the language used in the Regulation evokes similarities to the previously recognised category of utility tokens.[19] However, these tokens have been subsumed under the newly introduced category labelled "crypto-assets other than asset-referenced and e-money tokens". This broad category serves as a catch-all for various forms of crypto-assets that do not fit neatly into the more narrowly defined categories of "e-money" and "asset-referenced tokens".

15 Art. 3(7) of the MiCA Regulation defines e-money tokens as a type of crypto-asset that purports to maintain a stable value by referencing the value of one official currency.

16 Art. 3(6) of the MiCA Regulation defines asset-referenced tokens as a type of crypto-asset that is not an electronic money token and that purports to maintain a stable value by referencing another value or right or a combination thereof, including one or more official currencies.

17 Recital 18 notes that the third type consists of crypto-assets other than asset-referenced tokens and emoney tokens, and covers a wide variety of crypto-assets, including utility tokens.

18 For earlier classification efforts before the enactment of the MiCA Regulation see Valeria Ferrari, 'The regulation of crypto-assets in the EU – Investment and payment tokens under the radar' [2020], 27 Maastricht J. Eur. Comp. Law, 325.

19 Art. 3(9) of the MiCA Regulation defines utility tokens as a type of crypto-asset that is only intended to provide access to a good or a service supplied by its issuer.

At first glance, the older classification category of investment assets seems to be conspicuously absent from the framework of MiCA.[20] However, this striking omission is only superficial. In reality, Article 2(4) of MiCA provides a negative definition to delineate the outer limits of the scope of application of the Regulation. This provision specifies that MiCA does not apply to an exhaustively detailed list of crypto-assets, most notably assets that qualify as financial instruments. Effectively, Article 2(4) excludes investment assets from the scope of MiCA.[21] It is imperative to emphasise that although the exclusion of investment assets from the scope of the MiCA Regulation might appear straightforward on paper, this delineation may lead to significant practical challenges in its implementation. This complexity can be attributed to a variety of factors. One of the principal issues is the absence of harmonised definitions for certain concepts related to EU capital markets law. Notably, this includes the definition of "transferable securities" as outlined under Article 4(1)(44) of the MiFID II Directive.[22]

The ambiguity surrounding the definition of transferable securities has long been a topic of concern among scholars and practitioners alike, with the problem being extensively discussed in the literature that predates the enactment of the MiCA Regulation.[23] The European Securities and Markets Authority (ESMA) has also acknowledged the existence of these definitional ambiguities,

20 Before the enactment of the MiCA Regulation, scholarly debates revolved mainly around the question whether crypto-assets might qualify as "transferable securities" according to art. 4(1)(44) of the MiFID II Directive. For a detailed account see Phillip Hacker and Chris Thomale, 'Crypto-Securities Regulation: ICOs, Token Sales and Cryptocurrencies under EU Financial Law' (2017) <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3075820> accessed 23 April 2024.

21 See Recital 9 of the MiCA Regulation, where it is stated that Union legislative acts on financial services should be guided by the principles of 'same activities, same risks, same rules' and of technology neutrality. Therefore, crypto-assets that fall under existing Union legislative acts on financial services should remain regulated under the existing regulatory framework, regardless of the technology used for their issuance or their transfer, rather than this Regulation. Accordingly, art. 2(4) of the MiCA Regulation expressly excludes from its scope crypto-assets that qualify as financial instruments.

22 On the problem of definitional uncertainty in EU capital markets law, especially as regards the notion of transferable securities and its application to crypto-assets see Rüdiger Veil, European Capital Markets Law (3rd edn, Hart Publishing 2022) 165–166 and 186.

23 See, for example, Filippo Annunziata, 'Speak, If You Can: What Are You? An Alternative Approach to the Qualification of Tokens and Initial Coin Offerings' (2020) ECFR 129, Katja Langenbucher, 'European Securities Law – Are we in need of a new definition? A thought inspired by initial coin offerings' (2018) RTDF 40.

highlighting the regulatory challenges they pose, especially for the universe of crypto-assets.[24]

Recognising the practical difficulties that such definitional inconsistencies can create, the legislator has attempted to address these issues, at least to a certain extent, within the framework of the MiCA Regulation. This is evidenced by Recital 14, which explicitly mandates ESMA to issue detailed guidelines on the criteria and conditions necessary to qualify crypto-assets as financial instruments.[25] This mandate reflects a clear legislative intent to ensure that the classification of crypto-assets is not left completely to *ad hoc* interpretations but is guided by relatively standardised criteria that aim to foster consistency and predictability in regulatory practices across the EU. Nonetheless, accomplishing this task may prove to be quite challenging, not only because of the traditional divergences that plague the different national interpretations of the notion of "transferable securities" within the EU but also because of the dynamic nature of crypto markets and the often complex character of the assets traded within them.[26]

Two final observations are necessary in order better to understand the scope of application of the MiCA Regulation: a) the Regulation does not, in principle, regulate the offering of Non-Fungible Tokens (NFTs),[27] and b) the

24 See in detail European Securities and Markets Authority, 'Advice on Initial Coin Offerings and Crypto-Assets' (ESMA50-157-1391, Digital Finance and Innovation, Report) <https://www.esma.europa.eu/sites/default/files/library/esma50-157-1391_crypto_advice.pdf> accessed 23 April 2024.

25 Recital 14 states that for the purposes of ensuring a clear delineation between, on the one hand, crypto-assets covered by MiCA and, on the other hand, financial instruments, ESMA should be mandated to issue guidelines on the criteria and conditions for the qualification of crypto-assets as financial instruments.

26 Quite interestingly, Recital 14 puts the burden of the correct characterisation of crypto-assets on the issuers of such assets. This adds a further layer of complexity for market participants.

27 See art. 2(3) of the MiCA Regulation. Although the exclusion of NFTs appears as per art. 2(3) straightforward, Recital 11 complicates the exact limits of it. In essence, Recital 11 suggests that only NFTs that are truly non-fungible should escape the regulatory scope of the MiCA Regulation. Nonetheless, making a distinction between truly non-fungible assets and assets that appear non-fungile but are, in reality fungible, might not be as easy in practice, especially taking into account that the notions of "fungibility" and "non-fungibility" are not defined within MiCA. For an interesting overview of the complexities in defining the "fungible" or "non-fungible" nature of NFTs see Antonia Von Appen, 'US and EU Regulation on Fractionalized NFTs – Navigating Unchartered Waters' (21 December 2022) SSRN <https://ssrn.com/abstract=4308892 or http://dx.doi.org/10.2139/ssrn.4308892> accessed 23 April 2024.

Regulation does not apply to crypto-assets that are issued in a "fully" decentralised manner.[28]

3 The Offering of Title II Crypto-Assets (Assets Other than Asset-Referenced and E-money Tokens)

3.1 *The Precise Scope of Application of Title II*

Assets other than asset-referenced or e-money tokens are addressed in Title II of the MiCA Regulation. Systematically, they represent the default asset category of the Regulation, as Title II governs those crypto-assets that do not qualify as asset-referenced or e-money tokens. Typically, this encompasses all crypto-assets that do not aim to stabilise their price by referencing another asset.

At first glance, the title of Title II and the limited scope of Titles III and IV, which specifically cover certain types of stablecoins, might suggest that the category of crypto-assets other than asset-referenced or e-money tokens would encompass the majority of crypto-assets available in the market.

However, this assumption could not be further from the truth. Despite its expansive language, Title II incorporates several exclusions that significantly narrow its application. These exceptions are detailed in Article 4(3) of the MiCA Regulation.[29] To this list of exceptions from Title II, one should add the exception of NFTs from the overall scope of application of the Regulation since NFTs would otherwise fall within Title II of MiCA.

These exclusions are justified by the legislator's intention to adopt a more proportional regulatory approach.[30] This suggests that, in practice, the provisions of Title II should not apply to crypto-assets that do not present the fundamental regulatory risks that the Title aims to mitigate. Most regulatory

28 See Recital 22 of the MiCA Regulation. This highlights another area where interpretative and application challenges are anticipated. MiCA does not clearly define the concept of decentralisation, nor does it establish explicit benchmarks for assessing whether a crypto-asset is issued in a "fully" decentralised manner. For a brief discussion of the problem see Dirk Andreas Zetzsche and Julia Sinnig, 'The EU Approach to Regulating Digital Currencies' (16 January 2024) <https://ssrn.com/abstract=4707830> accessed 23 April 2024, 21.

29 Art. 4(3) foresees the following exceptions from Title II: (a) the crypto-asset is offered for free; (b) the crypto-asset is automatically created as a reward for the maintenance of the distributed ledger or the validation of transactions; (c) the offer concerns a utility token providing access to a good or service that exists or is in operation; (d) the holder of the crypto-asset has the right to use it only in exchange for goods and services in a limited network of merchants with contractual arrangements with the offeror.

30 See Recital 26 of the MiCA Regulation.

measures in Title II appear to address informational asymmetries between the issuers and crypto-asset holders.[31] No such risks seem to be present when crypto-assets are, for instance, offered for free, and the same is true for crypto-assets that are automatically generated as rewards for maintaining the distributed ledger or for validating transactions over the network.

This latter exemption is particularly significant as it effectively describes the primary process under which traditional cryptocurrencies like Bitcoin or Ether are produced and distributed. They both seem to fit the description of the exception established in Article 4(3)(b) of the MiCA Regulation. Teleological reasons seem to support this conclusion. Since miners and validators are rewarded with crypto-assets (e.g. Bitcoin or Ether) for the services they provide—namely, network maintenance and transaction validation—it would seem disproportionate to apply to such transactions compliance rules aimed at mitigating information asymmetries. Consequently, typical cryptocurrencies used as remuneration against the computational activities that maintain a blockchain ecosystem should generally not fall under MiCA.[32]

While the issuance of all the assets excluded from the scope of MiCA, in general, and Title II, in particular, is not regulated, it must be stressed that the provision of services concerning such excluded assets will still fall under Title V of the MiCA Regulation. In this way, these excluded crypto-assets are indirectly regulated at the level of service providers, ensuring some level of oversight and consumer protection despite the lack of direct Regulation of the activities related to their issuance.

3.2 *Compliance Requirements for Those Issuing Title II Crypto-Assets*

3.2.1 White Paper Drafting

The previous observations on the scope of Title II of the MiCA Regulation allow an attempt at an overview of the key regulatory decisions embedded within Title II. At a general level, it could be noted that Title II of the MiCA Regulation largely mirrors the disclosure regime found in traditional capital

31 See Recital 24 of the MiCA Regulation.

32 For a different assessment see Matthias Lehmann, 'MiCAR – Gold Standard or Regulatory Poison for the Crypto Industry?' (European Banking Institute Working Paper Series No 160, 12 January 2024) SSRN <https://ssrn.com/abstract=4692743> accessed 23 April 2024, 4. Lehmann assumes that typical cryptocurrencies such as Ether are covered by MiCA, yet he does not specify which Title he believes is applicable to them. However, his stance may be challenging to substantiate given the exclusion provided by art. 4(3)(b) of the MiCA Regulation, which he appears not to address in his discussion.

markets legislation, most notably the Prospectus Regulation.[33] The conditions under which such activities may be conducted are detailed in Article 4(1), which mandates that a person shall not make an offer to the public of a crypto-asset other than an asset-referenced token or e-money token within the Union unless he/she:

a. is a legal person;
b. has drawn up a crypto-asset white paper concerning that crypto-asset per Article 6;
c. has notified the crypto-asset white paper per Article 8;
d. has published the crypto-asset white paper per Article 9;
e. has drafted the marketing communications, if any, concerning that crypto-asset per Article 7;
f. has published the marketing communications, if any, concerning that crypto-asset per Article 9 and
g. complies with the requirements for offerors laid down in Article 14.

Notably, the issuance of Title II assets is restricted to legal persons, meaning that spontaneous issuances by *ad hoc* digital groups, previously common in the market, are no longer permitted. Significantly, the drafting and publication of a white paper become mandatory requirements. This reflects a practice already prevalent among most developer teams producing crypto-assets in the past, where white papers were typically issued primarily as marketing tools. This marketing tool has now been formalised into a mandatory requirement.

In addition to codifying formerly voluntary industry practices, Article 4 aligns MiCA more closely with the disclosure regime of the Prospectus Regulation. This alignment confirms that crypto-assets under Title II must display some financial use to be regulated. This is because prospectus disclosures are typically required for assets that are traded on financial markets and thus could give rise to informational asymmetries.[34]

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33 European Parliament and Council of the European Union, 'Regulation (EU) 2017/1129 of 14 June 2017 on the Prospectus to be Published When Securities are Offered to the Public or Admitted to Trading on a Regulated Market, and Repealing Directive 2003/71/EC' [2017] OJ L 168/12.

34 See Recital 3 of the prospectus Regulation which assumes that disclosure of information in cases of offers of securities to the public or admission of securities to trading on a regulated market is vital to protect investors by removing asymmetries of information between them and issuers. When it comes to Title II of MiCA, its regulatory alignment with the Prospectus Regulation is supported already in Recital 24, which specifically speaks of mandatory disclosures for the offering of Title II crypto-assets. The same conclusion is further supported by the provision of art. 4(2) of MiCA which exempts from the obligation of drafting a white paper the following offers of Title II crypto-assets: a) an offer to fewer than 150 natural or legal persons per Member State where such persons are

Notably, the white paper does not require approval from the supervisory authority, and the person offering the crypto asset is not subject to any licensing regime. This reflects a lighter touch approach to Title II assets, likely indicating that the legislator does not view their risks to market integrity and consumer protection as severe enough to necessitate mandatory licensing of the offeror or approval of the white paper by the supervisory authority. However, legal persons offering a Title II asset must notify the white paper's supervisory authority.[35] The content and format of the white paper are detailed in Article 6 and Annex I of the MiCA Regulation, while Article 7 governs marketing communications.

3.2.2 Holder Rights and Liability

A significant component of the regulatory framework in Title II is the provision of certain rights to the holders of Title II assets, among which the right of withdrawal, established in Article 13, stands out as particularly crucial.[36] According to Article 13, retail holders who purchase crypto-assets other than asset-referenced tokens and e-money tokens, whether directly from an offeror or through a crypto-asset service provider acting on behalf of the offeror, are entitled to an unjustified and cost-free withdrawal. This right must be exercised within 14 days from the retail holder's agreement to purchase the crypto-assets. Exercising this right results in the termination of the contractual relationship between the legal person offering the asset and the retail holder, along with the reimbursement of any payments made for its acquisition. Crucially, offerors must inform retail holders about the right of withdrawal in the white paper, ensuring transparency and safeguarding consumer rights within this regulatory context.[37]

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acting on their own account; (b) over a period of 12 months, starting with the beginning of the offer, the total consideration of an offer to the public of a crypto-asset in the Union does not exceed EUR 1 000 000, or the equivalent amount in another official currency or in crypto-assets; (c) an offer of a crypto-asset addressed solely to qualified investors where the crypto-asset can only be held by such qualified investors. The wording of the provision demonstrates that these exceptions closely reflect those outlined in art. 1(4) of the Prospectus Regulation, thereby confirming the genealogical relationship between the two regulatory frameworks.

35 See art. 8 of the MiCA Regulation.

36 Especially because it constitutes the basic mechanism that enhances the protection of retail holders within Title II of the MiCA Regulation. See in that light Recital 37 of the MiCA Regulation.

37 See art. 13(3) of the MiCA Regulation.

Another noteworthy regulatory decision is articulated in Article 15, which concerns the liability of offerors for the content of the white paper.[38] According to Article 15, if an offeror, a person seeking admission to trading, or an operator of a trading platform provides incomplete, unfair, unclear, or misleading information in their crypto-asset white paper or a modified version, then that offeror, along with the members of its administrative, management, or supervisory bodies, shall be liable to a holder of the crypto-asset for any losses incurred due to that misinformation.

This provision offers several interesting points for consideration.[39] Firstly, the scope of the liability regime is notably broad, encompassing not only the offeror or the person seeking admission to trading but also potentially the operators of trading platforms and members of their administrative, management, or supervisory bodies. Secondly, the concept of civil liability for the content of a white paper is not novel—since the Prospectus Regulation also includes similar provisions—Article 15 establishes such liability directly, without the need for reference to the national civil laws of the Member States. In other words, the basis of liability is already established under EU law. However, Article 15 leaves several details unspecified, and some supplementary applications of the national civil law of the Member States might not be entirely precluded. Nonetheless, this is an autonomous civil liability provision within an EU Regulation, and national law should not undermine its independent interpretation and application, although maintaining the necessary balance here might prove to be a challenging task.

3.2.3 Title II Outlook

Overall, the provisions of Title II appear to represent a lighter variant of the conventional disclosure regime typically applicable to transferable securities. There are several intriguing innovations, such as the right of withdrawal outlined in Article 13 and the structure of the autonomous civil liability specified in Article 15. However, Title II seems to be a less stringent disclosure regime specifically adapted to the unique characteristics of crypto markets. In this respect, crypto-assets are afforded a more flexible regulatory framework, suggesting that the legislator aimed to provide a structured yet accommodating environment. This approach indicates a desire to offer some regulatory

38 Recital 39 considers that the main reason behind the adoption of the provision of art. 15 is the protection of retail holders of Title II crypto-assets.

39 For an overview see Filippo Annunziata, 'An Overview of the Markets in Crypto-Assets Regulation (MiCAR)' (European Banking Institute Working Paper Series No 158, 11 December 2023) SSRN <https://ssrn.com/abstract=4660379> accessed 23 April 2024, 44.

oversight while avoiding overly burdensome regulations that could stifle the fundamental market dynamics for crypto-assets.

4 The Offer of Stablecoins

4.1 *General Observations*

Stablecoins are undeniably at the core of the regulatory issues addressed by MiCA. This should not be surprising since stablecoins play a crucial role within the crypto ecosystem.[40] In effect, they serve as the unofficial banking system of the crypto world, providing a platform for users to hold or move their crypto assets within a more stable pricing environment, thereby mitigating price volatility. Moreover, stablecoins function as a conduit between crypto-currencies and official currencies, bridging a gap left by traditional banking institutions, which are typically hesitant to facilitate crypto transactions. Stablecoins also hold the potential to act as a global payment method, particularly in countries with weak currencies and high inflation rates or even in advanced economies where big tech companies can dominate the financial landscape. Additionally, stablecoins are frequently used for leverage; crypto investors often borrow stablecoins to finance specific positions within the broader crypto asset universe. This multifaceted utility underlines the significance of stablecoins and the necessity for their careful Regulation as outlined in MiCA, ensuring they contribute positively to the financial ecosystem while mitigating potential risks associated with their use.

At a very abstract level, a fundamental characteristic that defines the risk profile of stablecoins is the method by which they achieve price stabilisation. One can distinguish between collateralised and non-collateralised stablecoins.[41] Collateralised stablecoins aim to maintain a stable value by holding sufficient reserves that support the stablecoin's peg to an official currency or another asset with relatively stable value. In contrast, non-collateralised stablecoins do not have reserves. Instead, these stablecoins use algorithms to facilitate trading arbitrage between the stablecoin and a twin fluctuating asset

40 For a detailed account see Mitsu Adachi, Pedro Bento Pereira Da Silva, Alexandra Born and others, 'Stablecoins' Role in Crypto and Beyond: Functions, Risks and Policy' <https://www.ecb.europa.eu/press/financial-stability-publications/macroprudential-bulletin/html/ecb.mpbu202207_2~836f682ed7.en.html> accessed 23 April 2024.

41 For a detailed exploration of the different types of stablecoins see Adrien d'Avernas, Vincent Maurin, and Quentin Vandeweyer, 'Can Stablecoins Be Stable?' (University of Chicago, Becker Friedman Institute for Economics Working Paper No 2022–131, 19 September 2022) <https://ssrn.com/abstract=4226027> accessed 23 April 2024.

to maintain a stable value. The risks associated with collateralised stablecoins primarily concern their reserves' composition, quantity, and management.[42] In contrast, the risks for algorithmic stablecoins revolve mainly around the stabilisation mechanism of the algorithm and the potential for death spiral risks.[43]

MiCA aims to regulate both stablecoins, although the primary regulatory framework and patterns outlined in Titles III and IV seem to be tailored to collateralised stablecoins. This has sparked some debate on whether MiCA regulates algorithmic stablecoins at all. Some commentators argue that offering algorithmic stablecoins is unfeasible under Titles III and IV of MiCA.[44] However, this argument is not entirely accurate, nor is it incontrovertible. Recital 41 of the MiCA regulation specifies that algorithmic stablecoins remain within the regulatory scope of MiCA and that there is no prohibition on their offering. Indeed, Recital 41 states that where a crypto-asset falls within the definition of an asset-referenced token or e-money token, Title III or IV of MiCA should apply, irrespective of how the issuer intends to design the crypto-asset, including any mechanisms for maintaining a stable value of the crypto-asset. This also applies to so-called algorithmic stablecoins that aim to maintain a stable value concerning an official currency or one or several assets through protocols that adjust the supply of such crypto-assets in response to demand changes.

While it is true that Titles III and IV are modelled after collateralised stablecoins, this does not imply that algorithmic stablecoins are excluded from the Regulation or that they are banned. The wording of Recital 41 allows for another interpretation, including algorithmic stablecoins within MiCA, but only to the extent that the provisions of Titles III and IV are compatible with their structural characteristics. This could mean, for example, that issuers of algorithmic stablecoins might need to obtain a licence under Titles III or IV of MiCA or that they should submit a white paper for authorisation. However, they should not be required to create and maintain a reserve of assets, as this would contradict the nature of their product.[45]

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42 See in more detail Cameron MacDonald and Laura Zhao, 'Stablecoins and Their Risks to Financial Stability' (Bank of Canada Staff Discussion Paper 2022–20, 28 November 2022) <https://ssrn.com/abstract=4466522> accessed 23 April 2024.

43 See Ariah Klages-Mundt and Andreea Minca, 'While Stability Lasts: A Stochastic Model of Noncustodial Stablecoins' (2022) 32(4) Mathematical Finance 943.

44 For example Lehmann (n 32), 18, who goes so far as to express the view that MiCA makes the offering of algorithmic stablecoins impossible.

45 See Edoardo D Martino, 'Regulating Stablecoins as Private Money between Liquidity and Safety. The Case of the EU "Market in Crypto Asset" (MiCA) Regulation' (Amsterdam Law School Research Paper No 2022–27, Amsterdam Center for Law & Economics

Given that collateralised stablecoins are the basic stablecoin phenotype regulated by MiCA and the fact that algorithmic stablecoins can mostly benefit from the basic provisions on authorisation and licensing, the rest of this section will focus on the key regulatory choices made by MiCA for collateralised stablecoins.

4.2 *Delineating the Scope of Title III and Title IV*

The first question in this context is how to delineate the scope of application of Titles III and IV, given that the legislator has established two distinct regimes depending on the specific nature of the collateralised stablecoin. More precisely, Title III regulates asset-referenced tokens, a category of crypto-assets that are not e-money tokens and aim to maintain a stable value by referencing another value, right, or a combination thereof, including one or more official currencies.[46] Conversely, Title IV deals with e-money tokens, defined as a family of crypto-assets that aim to maintain a stable value by referencing the value of a single official currency.[47]

A basic comparison between these two types demonstrates that although both categories are types of collateralised stablecoins, the difference lies in their price stabilisation method. What determines whether an asset falls within one category or the other? Suppose one interprets the definitions of asset-referenced tokens and e-money tokens quite literally. In that case, it might seem that the distinction between them is based on the asset to which they refer, in other words, their peg. For instance, if an asset is pegged to the US dollar, it would be classified as an electronic money token, whereas if it is pegged to Bitcoin, it would be considered an asset-referenced token. However, a closer examination suggests that the distinguishing factor is not merely the peg *per se* but the collateral and the composition of the reserves used to support the peg.[48] Only after one looks at both the peg and the collateral and composition

Working Paper No 2022–07, 30 August 2022) <https://ssrn.com/abstract=4203885> accessed 23 April 2024, 35. Martino also considers that the provisions of Titles III and IV of the MiCA Regulation might act as an obstacle to the issuance of algorithmic stablecoins. However, unlike Lehmann, he adopts a more nuanced approach, suggesting that it is conceivable to apply Titles III and IV to stablecoins, but only to the extent that they are compatible with their structure. He also posits that the requirements for authorisation and the drafting of a white paper could be applicable to algorithmic stablecoins, while the provisions concerning the reserve of assets would not apply to them.

46 See art. 3(6) of the MiCA Regulation.

47 See art. 3(7) of the MiCA Regulation.

48 For the same assessment see Matyáš Vilímek, 'Proposal for a Regulation on Markets in Crypto-Assets: Impact on Currently Available Stablecoins' (Master's thesis, Charles

of the reserves used to support it can a conclusion about the exact nature of a stablecoin be determined under MiCA.

This is crucial because, in practice, most stablecoins aim to maintain a stable value by referencing an official currency. It is conceivable, for example, that a stablecoin might reference the Euro yet deploy a reserve of gold to support its peg. Classifying this asset as an e-money token simply because it is pegged to the Euro while ignoring the reserves' composition could lead to inappropriate regulatory oversight. Indeed, if such an asset were to fall under Title IV of MiCA, the fundamental requirements regarding managing the reserve assets would be dictated by the Electronic Money Directive, to which Article 48(3) directly refers. However, the Electronic Money Directive is not an adequate regime to regulate a reserve composed of gold since it is tailored for reserves that consist of funds. Gold is not funds. A crypto asset that aims to maintain a stable value relative to the Euro by holding a reserve in gold would, therefore, be more appropriately regulated under Title III of the MiCA Regulation, where detailed rules are laid out on managing and maintaining such a reserve safely. In this context, the primary factor distinguishing Title III from Title IV should be the collateral and the composition of the reserve of assets that support the peg of a stablecoin and not only the peg *per se*.[49]

4.3 *Licensing and Authorisation*

Having delineated the basic scope of Titles III and IV, attention should turn to the safeguards established for such products by MiCA. The provisions of Title III are more detailed in this respect. At the same time, those of Title IV largely mirror those of Title III but with some notable exceptions, particularly

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University, Faculty of Law, Department of Financial Law and Financial Science, 2022) <https://dspace.cuni.cz/handle/20.500.11956/172535> accessed 23 April 2024, 43–46.

49 This conclusion is further supported by the original understanding of stablecoins during the legislative process that resulted in MiCA. See European Commission, 'Impact Assessment Accompanying the document Proposal for a Regulation of the European Parliament and of the Council on Markets in Crypto-assets and amending Directive (EU) 2019/1937' (SWD(2020) 380 final, 24 September 2020) (COM(2020) 593 final) - (SEC(2020) 306 final) - (SWD(2020) 381 final). In this original impact assessment of the Commission stablecoins are described as follows (p. 7): "… The "stablecoins" are a relatively new form of payment tokens with particular features aimed at stabilising their value. "Stablecoins" are typically backed by real assets or funds (such as short-term government bonds, fiat currencies …) or by other crypto-assets. They can also take the form of algorithmic "stablecoins" (with algorithm being used as a way to stabilise volatility in the value of the coin) …". It seems that the legislator understands the different categories of stablecoins on the basis of their collateral and not on the basis of their peg, since reference is being made on how they are "backed" and not on their peg per se.

concerning the composition and management of reserves. Consequently, the discussion will primarily focus on Title III, but cross-references between the two titles will be made where necessary to provide a comprehensive understanding of the regulatory framework.

A primary safeguard implemented by MiCA is that offering asset-referenced and e-money tokens is contingent upon the offerors being licensed. For asset-referenced tokens, licensing is required in accordance with Article 21 of MiCA. For e-money tokens, Article 48(1) stipulates that the offeror should be licensed as an electronic money institution. In either case, credit institutions can issue asset-referenced, or e-money tokens without any additional license or authorisation[50]provided they comply with Article 17 for asset-referenced tokens[51] or notify an e-money white paper as per Article 51 of MiCA for e-money tokens.[52] This regulatory approach may incentivise traditional financial institutions to enter the crypto universe.[53] Given that traditional credit institutions are already licensed and subject to rigorous compliance and supervisory requirements, the omission of an additional license to offer crypto-assets appears proportional and justifiable. This streamlined approach facilitates the integration of established financial entities into the crypto market while ensuring they adhere to high regulatory standards.

While the authorisation requirements for credit institutions or e-money institutions are similar to existing frameworks,[54] Title III of MiCA introduces specific rules for authorising issuers of asset-referenced tokens. The key provisions in this regard are Articles 18–20, which establish the authorisation procedure.

Article 18 specifies the information that must be included in the application for authorisation. Issuers are required to apply to the competent authority of their home Member State. According to Article 20, upon receiving an application for authorisation as referred to in Article 18, competent authorities must

50 It must be emphasised that credit institutions are only exempted from the licensing and authorisation requirements specified in Titles III and IV. However, they are still required to comply with all other obligations applicable to issuers of asset-referenced or e-money tokens. See, in that regard, Recital 44 of the MiCA Regulation.

51 See art. 16(1)(b) MiCA.

52 See see art. 48(1)(b) MiCA.

53 Recent reports from industry media imply that credit institutions might indeed be more open to crypto-assets and crypto services. See Zoltan Vardai, 'Europe's Largest Banks are Moving into Crypto Thanks to Regulations—Bitpanda' (Cointelegraph) <https://cointelegraph.com/news/european-banks-entering-crypto-bitpanda> accessed 23 April 2024. Nonetheless, it may be too early to reliably assess such trends.

54 See, for example, art. 8 of Directive 2013/36/EU for credit institutions and Title II of the Electronic Money Directive for e-money institutions.

assess within twenty-five working days of receipt whether the application, including the crypto-asset white paper mentioned in Article 19, contains all the required information. Interestingly, for asset-referenced tokens, it is not only mandatory to issue a white paper as per Article 19 but also forms part of the authorisation procedure. The competent authority must also approve it. This contrasts with Title II assets, where issuers only need to notify their white paper without it being subject to approval. However, similar to Title II, Titles III and IV also provide for civil liability in the event of inaccurate information in the white paper,[55] and such inaccuracies might even trigger the withdrawal of the overall authorisation.[56] The precise content of the white paper is detailed in Article 19.

Competent authorities must, within sixty working days of receiving a complete application, assess whether the applicant issuer complies with the requirements of this Title III and issue a fully reasoned draft decision granting or refusing authorisation. During these sixty working days, competent authorities may request additional information from the applicant issuer concerning the application, including details on the crypto asset white paper mentioned in Article 19.[57] This comprehensive evaluation process ensures that only those issuers meeting stringent criteria are authorised, thereby maintaining the integrity and stability of the financial market.

4.4 *Composition, Management, and Custody of the Reserve of Assets*

Arguably, the most crucial aspect of the regulatory framework for asset-referenced tokens revolves around the creation, composition, management, and custody of the reserve of assets. This focus is hardly surprising. The predominant risk associated with the stablecoin business model stems from the potential inability of issuers to fulfil the redemption rights of their asset holders. Current industry practices in this area are often found wanting, primarily due to the absence of a clear regulatory regime. As a result, issuers frequently fail to adequately safeguard the reserve of assets or convincingly fulfil redemption requests.

To mitigate this fundamental risk, Article 36 of the MiCA Regulation requires issuers of asset-referenced tokens to establish and maintain a reserve of assets at all times. The same requirement applies to issuers of e-money tokens.[58] For

55 See art. 26 and art. 52 of the MiCA Regulation.

56 See art. 24(1)(b) of the MiCA Regulation.

57 See art. 20(2) MiCA Regulation.

58 See art. 7 of the Electronic Money Directive by reference from art. 48(3) of the MiCA Regulation.

issuers of asset-referenced tokens, the reserve of assets must be composed and managed in such a way that (a) the risks associated with the assets referenced by the asset-referenced tokens are covered and (b) the liquidity risks related to the permanent rights of redemption of the holders are addressed.[59]

MiCA enforces strict rules regarding the reserve's composition, safeguarding, and management to ensure these outcomes. For instance, the reserve of assets must be legally segregated from the issuer's estate and the reserves of other asset-referenced tokens, protecting the holders' interests in accordance with applicable law. This segregation ensures that creditors of the issuers have no recourse to the reserve of assets, particularly in the event of insolvency.[60]

Issuers that offer two or more asset-referenced tokens to the public must operate and maintain segregated pools of reserves for each token, managing each pool separately.[61] Where different issuers offer the same asset-referenced token to the public, they must operate and maintain only one reserve of assets for that token. The management bodies of issuers must ensure effective and prudent management of the reserve of assets. The issuers must also ensure that a corresponding increase or decrease always matches the issuance and redemption of asset-referenced tokens in the reserve of assets.[62]

To mitigate price fluctuations and prevent potential redemption panics, MiCA requires issuers of asset-referenced tokens to have a clear and detailed policy describing the stabilisation mechanism of such tokens.[63] Furthermore, issuers must mandate an independent audit of the reserve of assets every six months.[64] This is critical, as current industry practices vary significantly in transparency, with some entities, such as Tether, being notably elusive about their reserves.

Detailed rules on the custody of the reserve of assets are included in Article 37, while Article 38 details the conditions under which the reserve can be invested. Issuers of asset-referenced tokens that invest part of the reserve of assets must only invest those assets in highly liquid financial instruments with minimal market risk, credit risk, and concentration risk.[65] Units in an undertaking for collective investment in transferable securities (UCITS) are deemed assets with minimal risk for Article 38(1), provided the UCITS invests solely in assets specified by the EBA in accordance with Article 38(5) and the issuer

59 See art. 36(1) MiCA Regulation.
60 See art. 36(2) MiCA Regulation.
61 See art. 36(5) MiCA Regulation.
62 Art. 36(6) MiCA Regulation.
63 Art. 36(8) MiCA Regulation.
64 Art. 36(9) and (10) MiCA Regulation.
65 Art. 38(1) MiCA Regulation.

ensures that the reserve of assets is invested to minimise concentration risk.[66] The financial instruments in which the reserve of assets is invested must be held in custody in accordance with Article 37.[67]

All these requirements concerning the reserve of assets aim to ensure the exercise of the redemption right established in Article 39 for holders of asset-referenced tokens.[68] Issuers must establish, maintain, and implement clear, detailed policies and procedures concerning this permanent right of redemption.[69] Upon request by a holder of an asset-referenced token, an issuer of such token shall redeem either by paying an amount in funds, other than e-money, equivalent to the market value of the assets referenced by the asset-referenced token held or by delivering the assets referenced by the token. Issuers shall establish a policy on such permanent right of redemption, setting the redemption procedure's exact terms.[70] Without prejudice to Article 46, the redemption of asset-referenced tokens shall not be subject to a fee.[71]

4.5 *Title III and Title IV Outlook*

In conclusion, the regulatory framework encapsulated within Titles III and IV of the MiCA regulation is designed to address the fundamental risks associated with stablecoins. By prioritising the safeguarding of redemption rights and the protection of the reserve of assets that support the peg, these provisions aim to enhance the stability and reliability of stablecoins. This focus is critical, ensuring that stablecoins, which serve as a bridge between traditional

66 Art. 38(2) MiCA Regulation.

67 Art. 38(3) MiCA Regulation.

68 Similarly, art. 49 of the MiCA Regulation establishes the redeemability of e-money tokens.

69 Art. 39(1) MiCA Regulation.

70 Art. 39(2) details these conditions which should include: (a) the conditions, including thresholds, periods and timeframes, for holders of asset-referenced tokens to exercise such right of redemption; (b) the mechanisms and procedures to ensure the redemption of the asset-referenced tokens, including in stressed market circumstances, as well as in the context of the implementation of the recovery plan set out in art. 46 or, in the case of an orderly redemption of asset-referenced tokens, under art. 47; (c) the valuation, or the principles of valuation, of the asset-referenced tokens and of the reserve assets when the right of redemption is exercised by the holder of asset-referenced tokens, including by using the valuation methodology set out in art. 36(11); (d) the conditions for settlement of the redemption; and (e) measures that the issuers take to adequately manage increases or decreases in the reserve of assets in order to avoid any adverse impacts on the market of the reserve assets. Where issuers, when selling an asset-referenced token, accept a payment in funds other than electronic money, denominated in an official currency, they shall always provide an option to redeem the token in funds other than electronic money, denominated in the same official currency.

71 See art. 39(3) MiCA Regulation.

financial systems and the evolving digital economy, operate within a secure and trustworthy environment.

5 Conclusion

The introduction of the MiCA Regulation marks a crucial step in the ongoing evolution of the regulatory landscape for crypto-assets. It represents a concerted effort to impose order and structure on a previously chaotic and largely unstable market. The necessity of MiCA stems from the urgent need to provide a coherent framework that not only fosters financial innovation but also ensures a high level of protection for investors and maintains the integrity of the financial markets.

The Regulation's key provisions and strategic choices reflect a deep understanding of the complex dynamics of the crypto markets. MiCA's comprehensive approach aims to balance promoting innovation in financial technology with rigorous safeguards that protect against systemic risks. This dual focus is essential in an era where digital finance rapidly transforms traditional financial practices and new products and technologies continuously emerge.

However, while MiCA is a significant advancement, it has challenges. One of the primary difficulties lies in delineating the exact scope of its application. The fluid and evolving nature of crypto-assets makes it particularly challenging to classify and define them within the rigid structures of financial Regulation. For instance, defining which crypto-assets constitute transferable securities, as per Article 4(1)(44) of the MiFID II Directive, is complicated by these assets' diverse and innovative characteristics.

Furthermore, the Regulation grapples with decentralisation, an ostensibly pursued hallmark of blockchain technology and an allegedly defining feature of many crypto projects. Determining what constitutes a decentralised issuer or service provider, and thus falls outside the purview of MiCA, poses a significant regulatory challenge.

Title II of MiCA, which sets out a light disclosure regime for non-stablecoin assets, exemplifies the legislator's intent to foster transparency as a form of protection. By requiring disclosures, the Regulation aims to enlighten investors and market participants about the nature and risks of the crypto-assets they are dealing with, thereby reducing the information asymmetry that often plagues these markets.

The Regulation of asset-referenced and e-money tokens under Titles III and IV addresses another core risk area—namely, the composition and

maintenance of the reserve of assets. These provisions ensure adequate safeguards against the risks that could arise if the reserves backing these tokens were improperly managed or were insufficient to cover the tokens' liabilities. This aspect of MiCA is particularly important for maintaining confidence in stablecoins, which are increasingly seen as bridges between traditional financial systems and the crypto world.

In summary, MiCA represents a welcome development in the regulatory landscape, addressing some of the inherent risks and uncertainties of the crypto market. It strives to protect investors and the broader financial system while providing a legal framework supporting innovation and growth. However, as with any pioneering regulatory effort, the practical application and effectiveness of MiCA will need to be closely monitored and adjusted in response to the rapidly evolving digital finance environment. Continued dialogue between regulators, industry participants, and other stakeholders will be essential to refine the Regulation and ensure it meets its objectives without stifling the innovative potential of the crypto markets.

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CHAPTER 9

Facing the Golem: Disruptive Technologies vs Democracy in the EU Digital Single Market

Giovanni Zaccaroni

Abstract

This contribution argues in favour of a regulatory framework that is aware of the threats to democracy and EU values arising from disruptive technologies. Regulation of technological innovations is an increasingly important aspect of the EU Internal Market, up to the point of shaping an entirely new field, the Digital Single Market. It is crucial to develop the regulation of technological innovations in a way that complies with EU values and does not undermine the democratic process. To develop thoughts and ideas on this subject, the paper will focus on defining disruptive technology's fundamental values and analysing the relevant body of EU secondary law. Then, the author seeks to assess the readiness of EU primary and secondary law with the risks and opportunities posed by disruptive technologies and outlines the importance of compliance with EU fundamental values for the strategic autonomy of the EU. Finally, the author presents some ideas to help the EU legal order fill the gap in the protection from threats to democracy and EU fundamental values that comes from disruptive technologies.

1 Introduction

Disruptive technologies are shaping the environment around us, changing how we interpret reality and how we work, live, and behave. The ambition to control and regulate disruptive technologies to avoid their abuse is rooted in humankind's history. One of the most fascinating examples is the Golem, a mythological figure whose traces can be found in the Bible and the Kabbalah.[1] The Golem is a humanoid of unknown origin, usually made of clay or mud, that its master can control through a hole in his mouth, where the master

1 Among the many references to technological innovation as 'the Golem', see H. Collins and T. Pinch, *The Golem: what you should know about science* (Cambridge University Press, 1993).

 | DOI:10.1163/9789004712119_011

places a piece of paper where he writes the orders.[2] This legend evokes the idea that most humans have of technology: magic-like instruments to whom we give orders. However, we do not entirely understand technology and we are often worried about losing control. There are different examples of technological innovation as the Golem, some of which are unexpected. The world wide web, social media and increasingly fast communications have disrupted our habits.[3] Artificial Intelligence is changing radically intellectual works. Crypto assets and decentralised finance are challenging at the roots of traditional banking and financial systems. Cybersecurity threats are more and more frequent at the individual as well as at the system level. The application of disruptive technologies thus is challenging our way of life. Moreover, doing that also challenges the very underpinning structure of our society: the values we regard as fundamental, and among them, democracy.

To further substantiate this claim it is sufficient to think how easier it is nowadays for policymakers to influence the opinion of voters. Artificial Intelligence allows politicians to write and to talk to different audiences in a language different from their original one. News manipulated *ad hoc* to foster a reaction from the public is also spread at unimaginable speed, as happens with the news coverage of migration flows in Europe. The interaction with voters and electors that once required time (to travel and meet the constituency) and research (to explain to the voters your reasons and positions) takes place at a fraction of its cost and a factorial of its speed. However, democracy is not only challenged by the potential disruption of the electoral process. It is also challenged regularly by undermining citizens' trust in traditional institutions by being less capable of securing employment, providing economic resources, and ensuring safety. If democracy as such is unable (or less able) to provide citizens with fundamental guarantees, then the structure of democratic society is challenged at its foundation.

However, similarly to what happened with the Golem, disruptive technologies are harmful to democracy only if their inventors, programmers, and users are allowed to do so. To avoid this, it is necessary to develop a technology compliant with democracy and fundamental values and to do so at the most appropriate level – the European Union. A fundamental research question dominates this paper: is it possible to ensure that disruptive technologies

2 For a more detailed account of the legend of the Golem, see E. Wiesel, *The Golem: the story of a legend* (Summit Book, 1983).

3 The Commission in 2021 proposed a directive, that is now under negotiations, on the rights of platform workers. See Proposal for a Directive of the European Parliament and of the Council on improving working conditions in platform work, COM/2021/762 final.

are designed in a way that is consistent with EU democracy and fundamental values?

To do so, the paper will focus on the definition of disruptive technologies within the EU internal market (Section 9.2), of fundamental values in primary EU law (Section 9.3) and the analysis of the relevant body of EU secondary law (Section 9.4). Then, in Section 9.5, I will outline the importance of compliance with EU fundamental values for the strategic autonomy of the EU. I will also try to assess the readiness of EU primary and secondary law to deal with the risks and opportunities posed by disruptive technologies. Finally, in Section 9.6, I will present some ideas that, in my opinion, can help the EU legal order to fill the gap in the protection from the threats to democracy and EU fundamental values that can arise from disruptive technologies.

2 Disruptive Technologies and the Digital Single Market

Disruptive technologies live within a very specific part of the EU internal market that, since 2015, has been defined by the European Commission as the Digital Single Market.[4] The Digital Single Market consists of a series of regulatory adaptations to prepare the traditional freedoms composing the EU internal market (goods, services and establishment, persons and capital) for the digital transformation.[5] Ultimately, the role played by technological innovations in the economic life of the EU and beyond will lead to the so-called 'fourth industrial revolution', the integration of digital technologies in most aspects of life.[6] The influence of disruptive technologies has profoundly changed the EU internal market: to provide an example, in 2022, a significant part of all sales made was done through e-commerce.[7]

Disruptive technologies can be defined in several ways, but, in general, they are understood to be different kinds of technologies that impact how our

4 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: A Digital Single Market Strategy for Europe, 6 May 2015.

5 See Art. 1, Decision (EU) 2022/2481 of the European Parliament and of the Council of 14 December 2022 establishing the Digital Decade Policy Programme 2030.

6 See generally: European Commission, *Capitalising on the benefits of the 4th industrial revolution*, 2018, https://data.europa.eu/doi/10.2777/588385.

7 According to a Eurostat survey, up to 6,7% of the turnover in market in sales was done online in 2022. See Eurostat, Digital economy and society statistics – enterprises, 2024, https://ec.europa.eu/eurostat/statistics-explained/index.php?title=Digital_economy_and_society_statistics_-_enterprises#Enterprises_using_social_media.

society works and functions. The main avenue in which our society works is, so far, the concept of 'trust'. Trust underpins the functioning of our society as well as the legal (lawyers and notaries), economic (banks), political (members of the parliament), and social (e.g., civil status certificates) spheres. Our society is characterised by intermediaries that we trust and can perform different tasks on our behalf. A sworn translator performs a translation on a document in a language we do not know, a bank transfers the money of our rent (or mortgage) to our landlord, a lawyer represents us in front of a court, and we, collectively, entrust politicians to act on our behalf.

Disruptive technologies can break the link of trust that connects us with our intermediaries and replace them – or at least aspire to replace them. Artificial Intelligence allows us to translate a document instantly (without a translator); a crypto asset allows us to move a currency without a bank; a blockchain certifies the exchange of documents or the propriety of an inventoried good without needing a notary.

It is true that some of the applications of these technologies are already among us and that they have not entirely 'disrupted' yet or are simply developing in an environment where these new intermediaries are replacing the old ones. For instance, this seems to be the case with digital platforms (both e-commerce and social media platforms). These applications of technologies are replacing traditional intermediaries without eliminating them. Still, we should ask ourselves if and how we can exert the same control on these new intermediaries (or disintermediaries) as traditional ones.[8]

3 Defining Fundamental Values in Primary EU Law in the Context Applicable to Disruptive Technologies

The values included in Article 2 TEU are the benchmark for my proposed analysis.[9] However, considering the specific character of the EU legal order, some of the values included in the list of Article 2 are more relevant than others. According to Article 2, "the Union is founded on the values of respect for human dignity, freedom, democracy, equality, the rule of law and respect for

8 One could point, perhaps, at the example of banking supervision and the depth that reached in the years after the economic crisis.

9 See generally T. Von Danwitz, 'Values and the Rule of Law: Foundations of the European Union – An Inside Perspective from the ECJ', *Potchefstroom Electronic Law Journal* (2018), pp. 1–17. T. L. Boekestein, 'Making Do With What We Have: On the Interpretation and Enforcement of the EU's Founding Values', *German Law Journal* (2022), 431–451.

human rights, including the rights of persons belonging to minorities". However, respecting human dignity and freedom is irrelevant to applying disruptive technologies.[10] This is because disruptive technologies in the EU internal market can rarely operate within the realm of the primary needs of persons (although, of course, we can imagine applications of disruptive technologies that can undermine freedom and human dignity). Democracy, equality, the rule of law and respect for human rights are, on the other side, extremely relevant in the vast majority of cases where disruptive technologies arise. Thus, democracy and the other EU values I described above must be considered fundamental in this endeavour.

Despite this premise, it must be said that the framework of the Lisbon Treaty appears to a certain extent to be outdated to reflect the challenges that disruptive technologies pose to EU fundamental values. In this sense, many soft law acts promoted by the EU institutions (and sometimes by the Member States) have supplemented the lack of direct reference in the Treaties to the risks and opportunities that disruptive technologies represent for the EU.[11]

In particular, two declarations have been promoted on the compliance of digital public services with the EU values and democratic principles: the Tallinn Declaration (Ministerial Declaration on e-Government)[12] and the Berlin Declaration on Digital Society and Value-based Digital Government.[13] These documents have been signed under the EU umbrella but do not represent EU acts. Thus, they have not been published in the Official Journal of the European Union. Although it is not *per se* a declaration, it is also worth noting that there is a specific communication by the Commission on a 'European Democracy Action Plan'.[14] This action plan describes how the digital transition is changing our democracy and to which extent this change produces effects. Another

10 This is not to underestimate or reduce the importance that these concepts have among the values included in art. 2 TEU. Rather, it is to advocate in favor of the need for a specific approach to EU values in the Digital Single Market.

11 On these declaration see C. Cocito, P. De Hert 'The use of declarations by the European Commission: 'careful with that axe, Eugene'', *Digital Constitutionalism* (2023) https://digi-con.org/the-use-of-declarations-by-the-european-commission-careful-with-that-axe-eugene/.

12 'eGovernement Declaration', signed inTallin on 6 October 2017. See https://digital-strategy.ec.europa.eu/en/news/ministerial-declaration-egovernment-tallinn-declaration.

13 'Declaration on Digital Society and Value-based Digital Government', signed in Berlin on 8 December 2020.

14 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on the European Democracy Action Plan, COM/2020/790 Final.

declaration has been promoted by the Portuguese Presidency of the Council in 2021, entitled 'Digital Democracy with a Purpose'.[15]

The last in this line of declarations is the 'European Declaration on Digital Rights and Principles for the Digital Decade', promoted jointly by the Parliament, the Council, and the Commission and adopted as an interinstitutional declaration.[16] This last declaration is perhaps the most important one, as it refers to EU values from the outset,[17] and it has an entire chapter (n. IV) devoted to democratic participation in the digital sphere.

Of course, the EU institutions and Member States' tendency to indulge in declarations instead of engaging in constructive debates around binding acts can be criticised. However, in light of the current limited framework of EU legislation mainly adopted for harmonising the EU internal market, it is unclear if much more can be done.[18] It might even be argued that there is a lack of a more explicit legal basis in the Treaties to allow the adoption of specific acts addressed to assess compliance of disruptive technologies with democracy and EU fundamental values. For this reason, in the next paragraph, I will analyse the EU secondary law applicable to disruptive technology to understand if it can be useful to develop technology compliant with the EU's fundamental values and democratic principles.

4 EU Secondary Law

This paragraph will assess if the secondary legislation either mentions or embodies an approach that protects democracy and EU values.

4.1 *Strategic Secondary Legislation on Disruptive Technologies Not Directly Mentioning Threats to EU Values and Democracy*

There are certain EU legal texts that, despite their strategic importance for disruptive technologies, do not explicitly mention the potential threat to democracy and other EU fundamental values. A notable example is the e-IDAS

15 'Declaration on Digital Democracy with a Purpose', signed in Lisbon on 1 June 2021.

16 European Declaration on Digital Rights and Principles for the Digital Decade, 2023/C 23/01.

17 *Ibid.*, Recital (1), (5) and (6). Paragraphs 12–15.

18 The market harmonization goal of the EU legal instruments to regulate disruptive technologies is given by the lack of a specific legal basis, that led the Commission to propose the vast majority of these instruments under the legal basis of Art. 114 TFEU.

regulation.[19] This regulation was negotiated between 2012 and 2013 and is applicable as of 2016. Still, digital identity is a key sector where the potential abuse of this technology can easily undermine the democratic process (e.g., the use of digital identity in voting procedures). Recently, the Commission proposed a recast of the regulation, but also, in the newly proposed text, there is no reference to the potential threats to democracy and EU values.[20]

A similar approach has been followed in the key regulatory framework applicable to crypto assets, particularly in regulating the market in crypto assets (MiCA).[21] MiCA seems not to be aware of the potential threats to democracy and EU values that can be realised through the use of crypto assets (e.g., potentially using them to create a parallel currency system). However, several exchanges have started cautiously delisting (or threatening to) stable coins and privacy coins based on compliance with the MiCA regulatory requirements, revealing that, perhaps, even without a direct reference to EU values and democracy, it is possible to pursue a similar aim.

4.2 *Artificial Intelligence*

The Artificial Intelligence (AI) Act is of strategic importance for the EU.[22] Artificial Intelligence is one of the four technologies the Commission regarded as critical for technological development in the EU.[23] In the AI Act, there are certain references to EU values and their importance for this regulatory instrument:

In Recital (28), for instance, it is acknowledged that "Aside from the many beneficial uses of Artificial Intelligence, that technology can also be misused and provide novel and powerful tools for manipulative, exploitative and social control practices". Then, the EU legislator continues in Recital (28) regarding manipulative practices, mentioning that "Such practices are particularly

19 Regulation (EU) No 910/2014 of the European Parliament and of the Council of 23 July 2014 on electronic identification and trust services for electronic transactions in the internal market.

20 Regulation (EU) 2024/1183 of the European Parliament and of the Council of 11 April 2024 amending Regulation (EU) No 910/2014 as regards establishing the European Digital Identity Framework.

21 Regulation (EU) 2023/1114 of the European Parliament and of the Council of 31 May 2023 on markets in crypto-assets.

22 Regulation (EU) 2024/1689 of the European Parliament and of the Council of 13 June 2024 laying down harmonised rules on artificial intelligence.

23 Commission Recommendation of 3.10.2023 on critical technology areas for the EU's economic security for further risk assessment with Member States.

harmful and should be prohibited because they contradict Union values of respect for human dignity, freedom, equality, democracy and the rule of law and Union fundamental rights, including the right to non-discrimination, data protection and privacy and the rights of the child".

Also, in Recital (61), it is acknowledged that "Certain AI systems intended for the administration of justice and democratic processes should be classified as high-risk, considering their potentially significant impact on democracy, the rule of law, individual freedoms as well as the right to an effective remedy and to a fair trial". This means that AI technologies involved in the democratic process will be regarded as 'high-risk' technologies and be subjected to the additional requirements of the AI Act.[24] In Annex III, where the high-risk AI systems are listed, is explicitly included: "Administration of justice and democratic processes: (a) AI systems intended to assist a judicial authority in researching and interpreting facts and the law and in applying the law to a concrete set of facts".

Also, after adopting the position in the first reading by the European Parliament, references to fundamental rights increased considerably.[25] In particular, reference to democracy and EU values has been reinforced in Recital (1), which now includes "fundamental rights as enshrined in the Charter of fundamental rights of the European Union (the 'Charter'), including democracy, the rule of law and environmental protection, against the harmful effects of AI systems in the Union, and to support innovation".

A new Recital (2) has also been included, which makes express reference to applying the Regulation according to democracy and fundamental rights.[26] Reference to democracy and EU values has also been added to several other recitals.[27]

Article 1 of the Regulation as amended by the European Parliament also references "fundamental rights enshrined in the Charter of Fundamental Rights, including democracy, the rule of law and environmental protection". These elements have surely reinforced the role of the AI Act and its potential to avoid the use of disruptive technologies to threaten democracy and EU values in

24 Art. 6(2), Regulation laying down harmonised rules on artificial intelligence, *cit.*

25 The proposal was the subject of extremely tense negotiations between the Council and the Parliament, and the text changed considerably from the Commission initiative.

26 Recital 2: "This Regulation should be applied in accordance with the values of the Union enshrined as in the Charter, facilitating the protection of natural persons, undertakings, democracy, the rule of law and environmental protection, while boosting innovation and employment and making the Union a leader in the uptake of trustworthy AI".

27 In particular, Recitals (27) and (62).

the Digital Single Market. However, it should be remembered that the overall rationale of the Regulation, as testified by its main legal basis, is to allow the safe production and commercialisation of goods and services that use Artificial Intelligence.[28]

4.3 *Digital Platforms*

The Digital Services Act package is the regulatory framework of digital platforms, composed of t Digital Services Act (DSA)[29] and the Digital Markets Act (DMA).[30] This package was proposed by the Commission to contain the power of large companies (Google, Apple, Meta, Amazon) having a considerable influence on the digital environment. However, while in the DMA (which, in nature, is eminently concerned with competition law), there is no reference to threats to democracy and EU values, and some references are still present in the DSA.

Recital (80) describes four categories of systemic risks that large platforms should evaluate.[31] In Recital (81), it is said that "A second category concerns the actual or foreseeable impact of the service on the exercise of fundamental rights, as protected by the Charter […]" and in Recital (82) "A third category of risks concerns the actual or foreseeable negative effects on democratic processes, civic discourse and electoral processes, as well as public security". These risks should be the subject of a specific risk-assessment procedure described in Article 34 of the DSA.[32]

Also, the Freedom of Media Act is very important for preventing the threats towards democracy and EU fundamental values from digital platforms and undermining media freedom.[33] In this case, the textual choice of

28 The legal basis of the Regulation is Art. 114.

29 Regulation (EU) 2022/2065 of the European Parliament and of the Council of 19 October 2022 on a Single Market For Digital Services.

30 Regulation (EU) 2022/1925 of the European Parliament and of the Council of 14 September 2022 on contestable and fair markets in the digital sector.

31 Recital (80), Regulation (EU) 2022/2065 "Four categories of systemic risks should be assessed in-depth by the providers of very large online platforms and of very large online search engines".

32 *Ibid*. Art. 34(1): Providers of very large online platforms and of very large online search engines shall diligently identify, analyse and assess any systemic risks in the Union stemming from the design or functioning of their service and its related systems, including algorithmic systems, or from the use made of their services.

33 Regulation (EU) 2024/1083 of the European Parliament and of the Council of 11 April 2024 establishing a common framework for media services in the internal market.

the Commission seems to be, in the vast majority of cases, to refer directly to the respect of fundamental rights rather than, at large, to EU values and democracy.[34]

4.4 *Cybersecurity*

This area, now extensively regulated at the EU level, also concerns the threats to democracy and EU values that can be produced via cyber-attacks. In Directive (EU) 2022/2555, Recital (70), it is said: "Large-scale cybersecurity incidents and crises at Union level require coordinated action to ensure a rapid and effective response because of the high degree of interdependence between sectors and Member States. The availability of cyber-resilient network and information systems and the availability, confidentiality and integrity of data are vital for the security of the Union and for the protection of its citizens, businesses and institutions against incidents and cyber threats, as well as for enhancing the trust of individuals and organisations in the Union's ability to promote and protect a global, open, free, stable and secure cyberspace grounded in human rights, fundamental freedoms, democracy and the rule of law".

In Directive (EU) 2022/2557 on the resilience of critical entities, Article 2(3) includes the potential threats to the rule of law in the classification of incidents under the Directive: "'incident' means an event which has the potential to disrupt significantly, or that disrupts, the provision of an essential service, including when it affects the national systems that safeguard the rule of law".

5 A Technology That Complies with EU Fundamental Values as an Element of EU Strategic Autonomy

The relevance of disruptive technologies for the EU legal order is particularly clear when we see the link between these technologies and the strategic autonomy of the European Union. It is important to distinguish strategic autonomy from national sovereignty or from the temptation to emancipate from globalization.[35] On the contrary, the strategic autonomy of the EU means that the

34 Although a reference to values is present in *Ibid*., Recital (2): [...] The Union should help the media sector seize those opportunities within the internal market, while at the same time protecting the values, such as the protection of the fundamental rights, that are common to the Union and to its Member States.

35 It should be recognised that there is a certain degree of ambiguity between the notion of strategic autonomy and sovereignty in "EU fashion", at least in the interpretation given by French commentators. See, *inter alia*, Y. Bertoncini, 'Quelle "souveraineté européenne" après la déclaration de Versailles?', *Schuman Papers* n°721 (2023), https://

EU and its Member States should be able to withstand fundamental threats (like pandemics, climate change and conflicts) without necessarily resorting to external help or the support of neighbour organisations. At the moment of writing in April 2024, the EU does not have a legal instrument explicitly devoted to assessing the compliance of disruptive technologies with democracy and EU values. Classic instruments used in the context of the protection of the rule of law are also not adequate for use in this situation, as they are mainly addressed to states. Thus, they cannot be used to target the application of specific disruptive technologies. Some instruments can be re-purposed, and others are currently being developed within this scope, considering the framework of international law within which the EU is currently moving.

5.1 *The Council of Europe Framework Convention on Artificial Intelligence*

The Council of Europe is adopting a Framework Convention on Artificial Intelligence, Democracy and the Rule of Law. This Convention has been drafted by an *ad-hoc* Committee on Artificial Intelligence, established by the Committee of Ministers under Article 17 of the Statute of the Council of Europe.[36] The final version of the text has been published on the Committee on Artificial Intelligence website and on the Council of Europe website.[37] The Secretary General of the Council of Europe, Marija Pejčinović Burić, publicly declared that the Framework Convention was finalised on 15 March 2024.[38]

Article 13 of the Convention, among many other instruments, refers to a seemingly new principle that might effectively act as the basis for protecting democracy in the digital environment. This is the principle of 'Safe innovation' and, in its latest version, reads: "With a view to fostering innovation while avoiding adverse impacts on human rights, democracy and the rule of law, each Party is called upon to enable, as appropriate, the establishment of controlled

www.robert-schuman.eu/fr/questions-d-europe/721-quelle-souverainete-europeenne-apres-la-declaration-de-versailles.

36 See Committee on Artificial Intelligence's Terms of Reference, version of 1 January 2024, https://rm.coe.int/terms-of-reference-of-the-committee-on-artificial-intelligence-cai-/1680ade00f.

37 Framework Convention on Artificial Intelligence, Human Rights, Democracy and the Rule Of Law, https://www.coe.int/en/web/artificial-intelligence/the-framework-convention-on-artificial-intelligence.

38 Statement by Marija Pejčinović Burić, 'Artificial Intelligence, Human Rights, Democracy and the Rule of Law Framework Convention'(15 March 2024) https://www.coe.int/en/web/portal/-/artificial-intelligence-human-rights-democracy-and-the-rule-of-law-framework-convention.

environments for developing, experimenting and testing artificial intelligence systems under the supervision of its competent authorities".

The EU Member States are all Parties of the Council of Europe, and the Framework Convention explicitly allows the European Union to join.[39] In light of that, this principle will likely display its effectiveness within EU law. It can be a valuable tool in the courts' hands to protect horizontal democracy and EU values.

5.2 *The Charter of Fundamental Rights of the EU Read Together with the Declaration on European Digital Rights and Principles*

Several fundamental rights protected by the Charter of Fundamental Rights can be valuable instruments to protect from abuses.[40] The reach of the Charter on the digital environment has also been recently supplemented by a Declaration on European digital rights and principles that can be an interesting tool for interpreting the Charter and other EU instruments.[41] With this reference, paragraph 1 explicitly mentions the commitment of the Parties of the Declaration to "a) strengthening the democratic framework for a digital transformation that benefits everyone and improves the lives of all people living in the EU" and "b) taking necessary measures to ensure that the values of the EU and the rights of individuals as recognised by EU law are respected online as well as offline". Paragraph 15 also mentions the role of digital platforms in supporting the democratic debate online.[42]

5.3 *The Fundamental Rights Impact Assessment in the Artificial Intelligence Act*

Another element that can reinforce the protection of democracy and EU values is the impact assessment on fundamental rights in the Artificial Intelligence Act.[43] The fundamental rights impact assessment is detailed under Article 27

39 Article 30, Framework Convention on Artificial Intelligence, *cit.*

40 See, for instance, the reference to fundamental rights in the Charter in the impact assessment of the European Commission for the proposal for a Regulation on Artificial Intelligence *cit*., 11.

41 European Declaration on Digital Rights and Principles for the Digital Decade, *cit.*

42 Paragraph 15, European Declaration on Digital Rights and Principles for the Digital Decade, *cit.* "Online platforms, particularly very large online platforms, should support free democratic debate online".

43 On this see A. Mantelero, 'The Fundamental Rights Impact Assessment (FRIA) in the AI Act: roots, legal obligations and key elements for a model template', (2024), available at *SSRN* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4782126.

of the AI Act and applies only to high AI-risk systems.[44] The impact assessment should be conducted *ex-ante,* and it provides for a series of elements to be included in it: a description of the deployer's processes and the period or frequency with which each high-risk AI system is intended to be used, the categories of natural persons and groups likely to be affected by its use, the specific risks of harm likely to have an impact on the categories of persons, a description of the implementation of human oversight measures, the measures to be taken where those risks materialise.[45] However, it is impossible to take for granted that under the label of fundamental rights are included the potential threats to democracy and other EU fundamental values. This is also because it is difficult to give a uniformly accepted definition of democracy.[46] However, before the AI act enters into force and is fully applicable (and this will not happen before 24 months from its entrance),[47] it is too early to speculate, and the situation should be assessed on a case-by-case basis.

5.4 *The EU Legal Framework and the Challenges That Disruptive Technologies Pose to EU Fundamental Values and Democracy*

Disruptive technologies – the Golem – undoubtedly pose several challenges to democracy in the EU legal order and, of course, beyond. Perhaps it is not by chance that cases of interference of technology and media in democratic life are becoming more and more evident. Without evoking the Cambridge Analytica case and its consequences, in the United Kingdom, which relatively recently left the bloc, an authoritative media outlet found a link between a famous social media platform and riots in specific areas of London.[48] Also, among many other episodes, recently, a very influential technology tycoon, Elon Musk, relaunched (with a comment) a tweet by an Italian account known to spread fake news (yet it has more than 300k followers on Twitter/X).[49]

With the exceptions mentioned above, the EU regulatory framework seems still unprepared to target the threats that can emerge from the exponential emersion of information that can manipulate the democratic environment. The examples of the declarations and communications with the Commission

44 Art. 6, Regulation laying down harmonised rules on artificial intelligence, *cit.*

45 *Ibid.* Art. 27.1 (a) to (f).

46 See A. Mantelero, *cit.*, 22.

47 Art. 113, Regulation laying down harmonised rules on artificial intelligence, *cit.*

48 BBC, 'Inside Tiktok's real-life frenzies – from riots to false murder accusations' (20 September 2023), https://www.bbc.com/news/technology-66719572.

49 Open Online, 'Sulle Ong e i salvataggi in mare Elon Musk ha dato risalto al bufalaro Radio Genoa' (20 September 2023) https://www.open.online/2023/09/29/ong-elon-musk-radio-genoa-fake-news-fc/. [available in Italian only]

and the Member States, as well as the reference to democracy and the rule of law included in the latest version of the AI Act, are commendable but still have very little practical value. Also, one can wonder to which extent any regulatory power (or even superpower, as Anu Bradford recently noted in her last book)[50] can have the ambition to limit the reach and influence of disruptive technologies with the sole help of the regulatory weapon. It should also be considered that, in the lack of an overarching legal framework, the digital powers might consider to self-regulate themselves, which is already happening to a certain extent.[51]

In light of the preliminary analysis conducted in this paper, it can be said that the resilience of the EU legal order to specific threats targeting democracy and EU fundamental values via disruptive technologies remains low. There is a persistent need to find solutions that allow the EU and national authorities to have better control of the digital space while at the same time protecting freedom of expression and association. This balance seems extremely difficult to attain, but this challenge needs to be faced.

6 Conclusion

There are a series of recommendations that can help make the EU primary and secondary framework more resilient to the challenges posed by the Golem of disruptive technologies.

The first is to foster interdisciplinarity. This implies the support of the dissemination of EU law and national constitutional law to categories that are involved in the development of the digital economy (as IT engineers) while, at the same time, disseminating among lawyers, judges and policymakers the relevant technical knowledge. This should mitigate the gap between technology and the law and policy environment. This solution, however, is perhaps too naïve and requires considerable time to be realised.

A second set of solutions is a potential Treaty change (including the EU Charter of Fundamental Rights), the unicorn of the law and policy debate at the EU level. All the actors involved are eager to evoke Treaty change, but no one wants to sit at the table and discuss this. At the same time, the Treaty change is being postponed to prioritise the accession of new members. Thus, the digital sphere seems likely to be left to secondary law.

50 A. Bradford, *Digital Empires: The Global Battle to Regulate Technology* (2023).

51 See the notorious case of the Meta Oversight Board, https://www.oversightboard.com/.

A third potential solution is to promote self-regulation, following the model of several digital platforms.[52] However, although useful, self-regulation does not guarantee compliance with the benchmark of the physical legal orders and could eventually facilitate the establishment of autonomous protection standards.

The last solution is to develop *ad-hoc* regulatory tools to promote compliance of disruptive technologies with democracy and EU fundamental values.[53] These regulatory tools – a first example might be the Council of Europe Framework Convention on Artificial Intelligence and human rights, democracy and the rule of law – should be guided by the set of values in EU primary law, as amended and enriched by the many declarations that intervened in the last few years, including the European Declaration on Digital Rights and Principles and the European Pillar on Social Rights. The downside of this approach is that it goes on top of the already existing impressive body of legislation on technology. It will likely take several years to be negotiated and implemented while potentially being received by the digital industry as problematic.

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52 M.A. Cusumano, A. Gawer, D. B. Yoffie, 'Can self-regulation save digital platforms?, *Industrial and Corporate Change*, (2021), 1259–1285, 1271.

53 There have been already early attempts, as the one mentioned by A. Mantelero, *cit*., p. 17 and developed by the Alan Turing Institute, 'Human Rights, Democracy, and the Rule of Law Assurance Framework for AI Systems: A proposal prepared for the Council of Europe's Ad hoc Committee on Artificial Intelligence' (2021) https://rm.coe.int/huderaf-coe-final-1-2752-6741-5300-v-1/1680a3f688.

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PART 3

Substantive Matters

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CHAPTER 10

Efforts Towards Achieving Effective and Adequate Remedies in Public Procurement for Better Functioning of the EU's Internal Market

Joseph Bugeja

Abstract

The Remedies Directives are intended to offer remedies to aggrieved tenderers in the public procurement process. Some aspects of the Remedies Directives, such as the review bodies involved in the judicial process and the heads of damages, call for more harmonisation. This will guarantee legal certainty and EU law's full direct uniform effect in the Member States. The divergent legal norms in the Member States prove that without the much-needed harmonisation of public procurement remedies, there is no effective legal protection for aggrieved tenderers. While one speaks of legal certainty, one rarely speaks of judicial certainty. For judicial certainty to be achieved, there has to be enhanced harmonisation of the review bodies and enhanced harmonisation of the damages awarded by these review bodies. Less effective remedies can lead to legal/judicial barriers, limiting the right of access to the Internal Market. Therefore, enhanced judicial protection in public procurement can contribute to the completion of the Internal Market by ensuring fairer and free competition, more open and non-discriminatory public procurement processes and an increase in cross-border trade within the Internal Market and with third countries.

1 The Importance of Barrier-Less Public Procurement in the EU's Internal Market

The EU's public procurement law and policy embrace the principles and procedures guiding contracting authorities and entities purchasing works, goods or services on the market. Public procurement law is intended to ensure that public funds are spent efficiently and quality is not jeopardised while obtaining the best price for the goods or services that are furnished. Fair, non-discriminatory, competitive, transparent and value-for-money tendering processes contribute

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to a country's economic development and sound financial management. In return, contracting authorities and economic operators reap economic benefits besides boosting international trade in goods and services, thus increasing economic growth.

The aim behind the public procurement directives[1] is to ensure the free movement of persons, goods, and capital in public procurement, including the freedom to provide services, non-discrimination on the grounds of nationality and equality of treatment.

Public procurement is perhaps one of the economic sectors which touches on all four free movements in the EU's internal market. The award of public tenders involves the supply of goods or services, or a combination of both, by economic operators in the EU Member States and also economic operators based in third countries who tender in the procurement market of the European Union.

Some tenders are purely for the supply of goods, such as computers for a particular government entity. There may be tenders, however, providing both for supply, namely the supply of computers and after-sales service or computer software services. In this case, the tender will be mixed for the goods and services supply. Some tenders are intended only to supply a contract of services, such as legal consultancy services. Tenders may also involve the free movement of persons. For instance, a tender for the supply of goods or services, or both, may include an element of free movement of persons, given that the preferred bidder may need to engage workers from another Member State or third country to pursue the public contract.

The same can be said of the free movement of capital. For tenders awarded across borders, the tenderer has the free movement of capital under the Treaty on the Functioning of the European Union, which applies to intra-EU and

1 The principal EU Directives on public procurement are the following:
   i. 'Directive 2014/23/EU of the European Parliament and of the Council on the award of concession contracts Text with EEA relevance' (2014) Official Journal L 94, 1–64.
   ii. 'Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC Text with EEA relevance (public sector)' Official Journal L 94, 65–242.
   iii. 'Directive 2014/25/EU of the European Parliament and of the Council of 26 February 2014 on procurement by entities operating in the water, energy, transport and postal services sectors and repealing Directive 2004/17/EC Text with EEA relevance (utilities sector)' Official Journal L 94, 243–37.

vis-à-vis third countries. It is the only free movement that applies to third countries.[2]

Therefore, the economic activity generated by public procurement depends on a fully functioning Internal Market in all areas of free movement.

Public procurement is increasingly becoming an important contributor to the EU's economy. According to the European Court of Auditors special report "Public procurement in the EU – Less competition for contracts awarded for works, goods and services in the ten years up to 2021", it is stated that:

> Some €2 trillion is spent on such procurement every year. This corresponds to approximately 14 % of the gross domestic product (GDP) of the EU's 27 member states, hereafter the "EU-27". Public procurement is thus one of the main drivers of economic growth and employment.[3]

The increased importance of the public procurement market for the EU Gross Domestic Product and its citizens further necessitates that any remaining barriers to trade in the Internal Market, including non-tariff barriers and, most importantly, the remedies regime, should be effective and adequate in order to incentivise more participation in the procurement market. This will translate into better choices, quality products and cheaper prices. This entails that tenders should be publicised as widely as possible, that direct orders should be kept at a minimum, and that the tendering process should conform as much as possible to the applicable EU law. Selection criteria must be non-discriminatory and transparent, while time-frames must be preserved.

The procurement process has to adhere to the fundamental principles of the Treaty, namely non-discrimination on the grounds of nationality (Article 18 TFEU), equal treatment, transparency and proportionality.

An important aspect of public procurement is that the remedies provided by the Remedies Directives must be effective. If the remedies are ineffective or insufficiently effective, they can pose a non-tariff barrier to trade, which hinders economic operators from participating in the tendering process. This study will examine whether the Remedies Directives are effective enough to

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2 Treaty on the Functioning of the European Union, Art 63:
"*1. Within the framework of the provisions set out in this Chapter, all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited.*
2. Within the framework of the provisions set out in this Chapter, all restrictions on payments between Member States and between Member States and third countries shall be prohibited".

3 European Court of Auditors, Special report "Public procurement in the EU – Less competition for contracts awarded for works, goods and services in the 10 years up to 2021", 6.

achieve real free movement of public procurement, judicial processes, and judgments in the Internal Market.

2 The Remedies Directives

Directive 89/665/EEC[4] and Directive 92/13/EEC,[5] as further amended by Directive 2007/66/EC[6] ('Remedies Directives'), are the available EU legal instruments to ensure that effective remedies are available in the Member States in instances where an aggrieved bidder who has participated in a public procurement process seeks redress. The Remedies Directives, being minimum Directives, leave much discretion to the Member States, which, coupled with the principle of judicial autonomy, leads to differences in providing effective remedies to injured bidders across the Member States. The Remedies Directives aim to coordinate the judicial remedies in the Member States as much as possible, with the ultimate aim being to reach uniform application, legal certainty and effective remedies in the Member States.

Besides providing effective remedies, the domestic laws of the Member States need to ensure that necessary checks and balances are adopted and maintained, such that decisions taken by the contracting entities are reviewed expeditiously to avoid further risks of possible award decisions infringing public procurement legislation. At the time of writing, i.e. April 2024, public procurement remedies and review bodies are essentially governed by the various national laws of the EU Member States. However, EU law requires the Member States to offer at least certain remedies whilst granting national systems discretion in determining and enforcing such remedies. Equal judicial protection is imperative in the EU's Internal Market so that all aggrieved bidders are treated equally, no matter in which jurisdiction they wish to challenge decisions they regard as unlawful. In order to achieve effectiveness, equivalence

4 Council Directive (EEC) 89/665 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 [1989] OJ L 395/30 (Directive 89/665/EEC).

5 Council Directive (EEC) 92/13 coordinating the laws, regulations and administrative provisions relating to the application of Community rules on the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors [1992] OJ L 76 (Directive 92/13/EEC).

6 Directive (EC) 2007/66 amending Council Directives 89/665/EEC and 92/13/EEC with regard to improving the effectiveness of review procedures concerning the award of public contracts [2007] OJ L 335 (Directive 2007/66/EC).

and uniformity in the remedies provided, it would perhaps be preferable to ensure protection at the EU level using a regulation rather than using the current Remedies Directives, which leave wide discretion to the Member States, to the disadvantage of claimants.

Ibi ius, ibi remedium – The Remedies Directives, Directive 89/665/EEC, Directive 92/1/3/EEC and Directive 2007/66/EC aim to ensure that Member States afford remedies in the field of public procurement. The preamble to Council Directive 89/665/EEC already sets the tone on what is intended in terms of remedies, namely that for them to have "tangible effects", they must be "effective and rapid".[7] Effectivity and rapidity have become even more important today, given that public procurement is increasingly becoming an important sector of the EU's economy.

That preamble laments that in some Member States, there is either the "absence of effective remedies" or the "inadequacy" of such remedies.[8] Today, we may have moved from the situation where remedies were absent. However, whether the remedies are 'adequate' and 'effective' enough is a very live issue, as is whether harmonising remedies in the Member States will be more conducive to effective remedies, thus increasing tenderers' faith in the tendering processes.[9]

The current Directives dedicated to remedies in connection with the public procurement process are the following:

i. 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;
ii. Council Directive 92/13/EEC of 25 February 1992 coordinating the laws, regulations and administrative provisions relating to the application of Community rules on the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors; and
iii. Directive 2007/66/EC of the European Parliament and of the Council of 11 December 2007 amending Council Directives 89/665/EEC and 92/13/EEC with regard to improving the effectiveness of review procedures concerning the award of public contracts.

Directive 2007/66 has introduced a standstill period, provisions pertaining to the ineffectiveness of public contracts, time limits, and alternative penalties.

7 Directive 89/665/EEC, Preamble.
8 *Ibid.*
9 *Ibid.*

The Remedies Directives provide aggrieved economic operators with three possible remedies, namely:

i. interim measures, including suspension of the procedure;
ii. the setting aside of decisions taken unlawfully, and
iii. damages granted to the person harmed by the infringement.[10]

Bovis has described the Remedies Directives as comprising "three fundamental principles: the principle of effectiveness, the principle of non-discrimination and the principle of procedural autonomy".[11] On the other hand, Arrowsmith has commented on the importance of legal remedies in the field of public procurement and the increased importance of such remedies when the subject of public procurement is assuming more relevance in modern economies:

> Under general principles of EU law, Member States must provide effective legal remedies to providers for enforcing the EU procurement rules. In practice, however, in the early days of the EU procurement regime, many states did not comply with this requirement and remedies that did exist were little used, in part because of legal uncertainty. In these circumstances, and because of the perceived importance of legal remedies in procurement, in the late 1980s/early 1990s the EU adopted specific directives to regulate procurement remedies in relation to contracts covered by the co-ordination directives.
> (…)
> These Remedies Directives apply to any alleged violations of EU law in award procedures governed by the Public Sector Directive or the Utilities Directive. *Inter alia*, they require Member States to provide specific types of remedies to aggrieved firms, namely interim measures, the setting aside of unlawful decisions and damages; and they also lay down rules on forum and procedure for bringing claims. The remedies that they provide were strengthened further by a directive adopted in 2007 (…)[12]

In a study led by the University of Nottingham under the project leadership of Professor Sue Arrowsmith, it was observed that the:

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10 *Ibid*., Article 1.

11 Christopher H. Bovis, *EU Public Procurement Law*, Elgar European Law, (Edward Elgar Publishing 2007) 371.

12 Sue Arrowsmith, *The Law of Public and Utilities Procurement – Regulation in the EU and UK*, Vol 1 (3rd edn, Sweet & Maxwell 2014) 178.

> Damages are not regulated in detail and their formulation does not contribute much to the creation of a clear legal situation and even generates doubts on some points. It is not even clear from these directives whether they require the possibility of an award on lost profit or not, which is of crucial importance for the efficiency of the remedy of damages. A high percentage of aggrieved tenderers do not consider it worthy of effort to initiate an action seeking to recover the costs of preparing a bid or participation in the procurement procedure. However, it is normally presumed in both theory and frequently in the case law of the Member States that tenderers under certain conditions can claim an award of lost profit for breach of the EU public procurement rules although this has been unclear from the outset.
>
> It is not clear from the wording of the Remedies Directives whether damages are available for all violations of the EU public procurement rules or whether other conditions apply. Article 2(1)(c) of the Remedies Directives indicates only that the Member States are obliged to award damages to persons harmed by the infringement. However, it is clear from the ruling of the European Court of Justice in C-275/03, *Commission v Portugal*, that it violates the Remedies Directive to make damages conditional on proof of intentional or negligent breach. The recent case C-314/09, *Stadt Graz,* is important as it seems to follow from this case that any breach in principle is sufficient ground for damages.[13]

However, since the *Stadt Graz v. Strabag AG and Others* judgment of 30 September 2010, the grounds of damages in public procurement have rapidly evolved, although inconsistently and uncertainly through the jurisprudence of the CJEU and the Member States' national courts, as will become apparent.[14]

3 Overview of Council Directive 89/665 (Public Sector)

The Directive applies to contracts referred to in Directive 2014/24/EU of the European Parliament and the Council (1) unless such contracts are excluded

13 Sue Arrowsmith, Paula Bordalo Faustino, Baudouin Heuninckx, Professor Steen Treumer, and Professor Jens Fejø, *EU Public Procurement: An Introduction* (University of Nottingham, 2011) 295–296.

14 Case C-314/09 *Stadt Graz v Strabag AG and Others* [2010] ECR I-8769.

in accordance with Articles 7, 8, 9, 10, 11, 12, 15, 16, 17 and 37 of that Directive.[15] It also applies to concessions awarded by contracting authorities, referred to in Directive 2014/23/EU[16] of the European Parliament and of the Council (2), unless such concessions are excluded in accordance with Articles 10, 11, 12, 17 and 25 of that Directive.[17]

The preamble to 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 notes that the:

> Opening up of public procurement to Community competition necessitates a substantial increase in the guarantees of transparency and non-discrimination; whereas for it to have tangible effects, effective and rapid remedies must be available in the case of infringements of Community law in the field of public procurement, or national rules implementing that law.[18]

Therefore, the drafters of the Directive have been very attentive in combining the principles of transparency and non-discrimination with the corollary principles of effectiveness and clarity of the remedies to be provided, which are of utmost importance to achieve a fully functional internal market in public procurement. Directive 89/665/EEC stipulates that the absence of effective remedies or inadequacy of existing remedies 'deter community undertakings from submitting tenders in the Member State where the contracting authority is established'.[19] This shows clearly that ineffective or inadequate remedies also hinder the Internal Market. Reference to this preoccupation with the level of 'effectiveness' of the remedies is also made by Bovis, where he comments that:

> The absence or inadequacy of effective remedies at national level has a detrimental effect in the opening up of public procurement by deterring undertakings from participating in award procedures for public contract and submitting tenders. The opening up of public procurement to Community-wide competition demands also a substantial increase in

15 Directive (EU) 2014/24/EU on public procurement and repealing Directive 2014/24/EU [2014] L 94/65.

16 Directive (EU) 2014/23/EU on the award of concession contracts 2014/23/EU [2014] L 94/1.

17 Directive 89/665/EEC, Article 1.

18 Directive 89/665/EEC, Preamble.

19 *Ibid.*

> the levels of transparency at national level regarding the availability of redress to the supply side of the public procurement equation (tenderers and participants). Such increased levels of transparency must be accompanied by non-discriminatory measures introduced within national legal systems which provide interested parties with at least the same treatment in public procurement litigation, as in other forms of litigation.[20]

Directive 89/665/EEC, besides commending "effective" and "adequate" remedies, given the short duration of the award procedure, also stressed that review bodies should have the *vires* to take interim measures to suspend the tendering process or the implementation of the contracting authority's decision, as the case may be. The short duration of the procedure also calls for urgency in the provision of remedies.

Member States must ensure that the contracting authorities' decisions are reviewed "effectively" and rapidly:

> Member States shall take the measures necessary to ensure that, as regards contracts falling within the scope of Directive 2004/18/EC, decisions taken by the contracting authorities may be reviewed effectively and, in particular, as rapidly as possible in accordance with the conditions set out in Articles 2 to 2f of this Directive on the grounds that such decisions have infringed Community law in the field of public procurement or national rules transposing that law.[21]

Member States must "ensure that the review procedures are available, under detailed rules which the Member States may establish".[22] However, Directive 89/665/EEC is not mandatory with respect to the first review of the aggrieved tenderer. It states that "Member States may require that the person concerned first seek review with the contracting authority",[23] in which case the Member State has to ensure that there is the "immediate suspension of the possibility to conclude the contract"..[24] The emphasis on the immediate suspension of the contract emanates from the fact that if the contract is awarded and concluded with the preferred economic operator despite the ongoing review proceedings,

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20 Christopher H. Bovis, *The Law of EU Public Procurement*, (2nd edn, Oxford University Press 2015) 493.

21 Directive 89/665/EEC, Article 1(3).

22 *Ibid.*

23 *Ibid.* Article 1(5), para 1.

24 *Ibid.*

then the aggrieved economic operator will be denied an effective remedy. Suppose there is no suspension of the conclusion of the contract. In that case, the aggrieved economic operator may have been granted the remedy, but certainly not an "effective" remedy, because the contract would have been concluded.

The " suspension " element mentioned in Directive 89/665/EEC "shall not end before the expiry of a period of at least ten calendar days".[25] The wording of the Directive could have been clearer and bolder in the sense that the suspension of the conclusion of the contract should endure until the final appeal is decided. Directive 89/665/EEC establishes the measures to be taken by the Member States to ensure review procedures. The list of review measures is not exhaustive and includes the following:

a. take, at the earliest opportunity and by way of interlocutory procedures, interim measures with the aim of correcting the alleged infringement or preventing further damage to the interests concerned, including measures to suspend or to ensure the suspension of the procedure for the award of a public contract or the implementation of any decisions taken by the contracting authority;
b. Either set aside or ensure the setting aside of decisions taken unlawfully, including the removal of discriminatory technical, economic or financial specifications in the invitation to tender, the contract documents or in any other document relating to the contract award procedure;
c. Award damages to persons harmed by an infringement[26]

In the Maltese Public Procurement Regulations 2016,[27] Regulation 90(3), there is a reference to article 2(1)(b) of Directive 89/665/EEC, whereby the first-instance Public Contracts Review Board ('PCRB') is empowered to "take such interim measures as it shall deem fit".[28] However, again, a reference to the setting aside or to ensure the setting aside of decisions is found in the provisions of the Public Procurement Regulations 2016 regulating specifically the area of pre-contractual remedies, namely:

25 *Ibid.* Article 1(5), para 3.
26 *Ibid.* Article 2(1).
27 Public Procurement Regulations 2016, Subsidiary Legislation 601.03, Laws of Malta (Public Procurement Regulations 2016).
28 *Ibid.*, Regulation 90(3).

> Prospective candidates and tenderers may, prior to the closing date of a call for competition, file a reasoned application before the Public Contracts Review Board:
>
> a. To set aside or ensure the setting aside of decisions, including clauses contained in the procurement document and clarification notes taken unlawfully at this stage or which are proven to be impossible to perform;[29]

Directive 89/665/EEC states that review procedures are to be 'effective' and that the review body's decisions must be "effectively enforced".[30] The Directive stops short on how the decisions can be "effectively enforced", and given the principle of judicial autonomy of the Member States, it is left in the hands of each Member State on how to enforce the decision. In Malta, for instance, decisions may be enforced through several executive warrants, provided in the Code of Organisation and Civil Procedure, Chapter 12 of the Laws of Malta.

Bovis, concerning the issue of enforcement, refers to the principle of judicial autonomy, which principle needs to take into consideration the principles of equivalence and effectiveness of decisions:

> The exercise of national procedural autonomy must respect the principles of equivalence and effectiveness. Article 1(3) of the Remedies Directive imposed an obligation on the Member States to ensure, under their own detailed rules, that review procedures are accessible at least to any person having or having had an interest in obtaining a particular contract and who has been or risks being harmed by an alleged infringement.
>
> The Member States are not obliged to make those review procedures available to any person wishing to obtain a public contract, but they may require that the person concerned has been or risks being harmed by the infringement he alleges.[31]
>
> (…)
>
> [I]n the absence of (Union) rules governing the matter, it is for the domestic legal system of each Member State to designate the courts and tribunals having jurisdiction and to lay down the detailed procedural rules governing actions for safeguarding rights which individuals derive directly from (Union) law, provided that such rules are not less favourable than those governing similar domestic actions (principle of equivalence) and that

29 *Ibid.*, Regulation 262(a).

30 Directive 89/665/EEC, Article 2(8).

31 Case C-249/01, *Hackermuller*, [2003] I-6319, para 18.

> they do not render practically impossible or excessively difficult the exercise of rights conferred by (Union) law (principle of effectiveness).[32]
>
> From the beginning it is important to distinguish between two situations. The *Telaustria* type of situation,[33] where co-ordinated rules on remedies were not applicable and the legal protection of individual rights derived directly from provisions of primary law, and the *Stadt Graz* type of situation,[34] where the applicable remedies are harmonised, meaning that the right to be awarded civil damages for infringements of public procurement law is specifically stipulated, thus not left to the discretion of the Member States.
>
> (…)
>
> [A] declaration that an application for damages, brought by the unsuccessful tenderer following the annulment of that decision by an administrative court, is well founded cannot – contrary to the wording, context and objective of the provisions of Directive 89/665 which establish the right to such damages – depend, for its part, on a finding that the contracting authority involved is at fault.[35,36]

Directive 89/665/EEC also provides that when a review body is not judicial, its decision must always contain written reasons. The decision of the non-judicial review body has to be subjected to the review of another review body "which is a court or tribunal within the meaning of Article 234 of the Treaty and independent of both the contracting authority and the review body".[37]

In Malta, this judicial function is performed by the Court of Appeal (Superior Jurisdiction), presided by the Chief Justice and two other judges, as per Regulation 284 of the Public Procurement Regulations 2016 whereby:

> Any party who feels aggrieved by a decision taken by the Review Board may appeal to the Court of Appeal as constituted in accordance with

32 Case C-543/99, *Courage & Crehan*, [2001] I-6297, *para* 29; see also Case C-91/08, Wahl AG, [2010] I-2815, para 65.

33 See Case C-324/98, *Telaustria and Telefonadress*, [2000] ECR I-10745.

34 Case C-314/09, *Stadt Graz v. Strabag AG*, [2010] I-8769; see also Case C-249/01, *Hackermuller* (n17); Case C-213/07, *Michaniki*, [2008] I-9999 concerning the rule that the grounds for exclusion must be open to review and Case C-470/99, *Universale-Bau and Others*, [2002] ECR I-11617 and Case C-241/06, *Lammerzahl*, [2007] I-8415 concerning the compulsory content of a contract notice or of the tender documents. C-314/01, *Siemens AG Osterreich*, [2004] I-2549 requires that clauses of a tender invitation must be open to review.

35 *Stadt Graz* (n 684).

36 Bovis (n 690) 498–500.

37 Directive 89/665/EEC, Article 2(9).

> article 41(1) of the Code of Organisation and Civil Procedure by means of an application filed in the registry of that court within twenty calendar days from the date on which that decision has been made public.[38]

This provision in Malta's Public Procurement Regulations 2016 is in line with Article 2(9) paragraph 2 of Directive 89/665/EEC whereby the members of the judicial independent body:

> shall be appointed and leave office under the same conditions as members of the judiciary as regards the authority responsible for their appointment, their period of office, and their removal. At least the President of this independent body shall have the same legal and professional qualifications as members of the judiciary. The independent body shall take its decisions following a procedure in which both sides are heard, and these decisions shall, by means determined by each Member State, be legally binding.[39]

By contrast, the Maltese Public Contracts Review Board (PCRB), which can be described as a quasi-judicial review body, comprises a chairperson and two permanent members appointed by the Prime Minister for three years, with the possibility of re-appointment.[40] However, there is no security of tenure, and the members are not constitutionally appointed, as judges and magistrates are. Furthermore, the chairman and members of the PCRB, unlike judges and magistrates who have a constitutional appointment, "shall not be precluded from exercising their profession. However, during their appointment, they shall be precluded from exercising their profession in cases before the Review Board".[41]

This is not considered an adequate safeguard to secure the independence and impartiality of the members of the Maltese PCRB.

4 Overview of Directive 2007/66/EC of 11 December 2007 (Amending Directive)

Following consultations with stakeholders, including contracting authorities and economic operators, aimed to ensure fairer and more competitive public procurement processes, Directive 2007/66/EC came into force, amending

38 Public Procurement Regulations, Regulation 284.
39 Directive 89/665/EEC, Article 2(9).
40 Public Procurement Regulations 2016, Regulation 81(1).
41 *Ibid.*, Regulation 86.

the prior Directives on Remedies. The rationale of Directive 2007/66/EC is to enhance the Member States' domestic review procedures for aggrieved economic operators who have been prejudiced by a public contract which has been unfairly awarded. In line with this rationale, at the time of the coming into force of Directive 2007/66/EC, Commissioner Mc Creevy[42] commented that:

> I am pleased that this Directive has been adopted so rapidly. We need effective procedures for seeking review in all EU Member States in order to make sure that public contracts ultimately go to the company which has made the best offer. By strengthening national review procedures in line with this Directive, businesses will have stronger incentives to bid for public contracts anywhere in the EU.[43]

Economic operators' rights have been substantially improved through this Directive, particularly:

- The contracting authorities have to abide by a standstill period of at least ten days, so that aggrieved economic operators will have the necessary time to decide on whether to request the review of the decision which has awarded the public contract;
- If the standstill period is not observed, the public contract may be deemed "ineffective";
- If the public contract remains in force for overriding reasons relating to a general interest, then alternative penalties must be applied.

5 Standstill Period

To achieve effective remedies, Member States must provide review procedures and allow "sufficient time for effective review of the contract award decisions taken by contracting authorities".[44] Thus, in article 2a(2) of Directive 2007/66/EC, at least ten calendar days must be allowed before the contract is concluded following its award. These ten days commence to run:

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42 Internal Market and Services Commissioner.

43 'Public Procurement: Commission welcomes adoption of Directive improving rights of rejected bidders' (European Commission, IP/07/1700, 15 November 2007).The European Commission proposed the Directive in May 2006 (IP/06/601). An agreement at first reading between European Commission, Council and the European Parliament was reached in June 2007 (IP/07/861).

44 Directive 89/665/EEC, Article 2a(1).

> from the day following the date of which the contract award decision is sent to the tenderers and candidates concerned if fax or electronic means are used or, if other means of communication are used, before the expiry of a period of either at least fifteen calendar days with effect from the day following the date on which the contract award decision is sent to the tenderers and candidates concerned or at least ten calendar days with effect from the day following the date of the receipt of the contract award decision.[45]

In order to ensure that the standstill period is respected, Directive 2007/66/EC stipulates that when the tenderer or the concerned candidate is informed about the award decision, the said communication should contain the following two requisites *ad validitatem*:

i. A summary of the 'relevant reasons' in concise form;
ii. "A precise statement of the exact standstill period applicable according to the provisions of national law transposing this paragraph".[46]

Article 2b of Directive 2007/66/EC provides for derogations from the standstill period. While article 2a refers to a standstill period with respect to the conclusion of contracts, article 2c relates to the time limits that need to be observed for:

> any application for review of a contracting authority's decision taken in the context of, or in relation to, a contract award procedure falling within the scope of Directive 2004/18/EC must be made before the expiry of a specified period, this period shall be at least 10 calendar days with effect from the day following the date on which the contracting authority's decision is sent to the tenderer or candidate if fax or electronic means are used or, if other means of communication are used, this period shall be either at least 15 calendar days with effect from the day following the date on which the contracting authority's decision is sent to the tenderer or candidate or at least 10 calendar days with effect from the day following the date of the receipt of the contracting authority's decision. In the case of an application for review concerning decisions referred to in Article 1(1)(b) of this Directive that are not subject to a specific notification, the time period shall be at least 10 calendar days from the date of the publication of the decision concerned.[47]

45 *Ibid.*, Article 2a(2).
46 *Ibid.*
47 Charter of Fundamental Rights on the European Union, Article 2c.

Baker and Mc Kenzie refer to this legal obligation to comply with the standstill periods enshrined in Directive 2007/66/EC and observe that while the contracting entities may set the time limits for the receipt of tenders, such time limits "may not be shorter than indicated in the EC directives on public procurement. Accelerated procedures may be followed in urgent cases where the time limits are impracticable".[48]

In *Universale-Bau AG, Bietergemeinschaft*, the Court (Sixth Chamber) referred to the importance of having reasonable time limits and observed that:

> 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, as amended by Council Directive 92/50/EEC of 18 June 1992 relating to the coordination of procedures for the award of public service contracts, does not preclude national legislation which provides that any application for review of a contracting authority's decision must be commenced within a time-limit laid down to that effect and that any irregularity in the award procedure relied upon in support of such application must be raised within the same period, if it is not to be out of time, with the result that, when that period has passed, it is no longer possible to challenge such a decision or to raise such an irregularity, provided that the time-limit in question is reasonable.[49]

In *Palmisani*, the Court (Fifth Chamber) held that the Member State has to satisfy reasonable time limits for there to be legal certainty:

> As regards the compatibility of a time limit of the kind provided for in the Legislative Decree with the principle of the effectiveness of Community law, the setting of reasonable limitation periods for bringing proceedings satisfies that requirement in principle, since it constitutes an application of the fundamental principle of legal certainty (see, in particular, Case 33/76 *Rewe*, cited above, paragraph 5).[50]

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48 Baker & Mc Kenzie, *Remedies and Public Procurement Laws in Europe*, (3rd edn, Baker & Mc Kenzie, 2009) 11.

49 Case C-470/99, *Universale-Bau AG, Bietergemeinschaft v. Entsorgungsbetriebe Simmering GmbH*, [2002] ECR I-11617.

50 Case C-261/95, *Rosalba Palmisani v Istituto nazionale della previdenza sociale* (*INPS*), [1997] ECR I-4025.

Article 2a (standstill period), article 2b (derogations from the standstill period) and Article 2c (time limits for applying for review) characterise an important element of Directive 2007/66/EC, which has amended Council Directives 89/665/EEC and 92/13/EEC. One of the aims of the amending Directive 2007/66/EC has been to strengthen the effectiveness of the remedies through more legal certainty with respect to the time limits allowed by law for the remedies. The amending Directive 2007/66/EC embodies the various rulings of the European Court of Justice with respect to the standstill periods, which rulings have now been harmonised:

> Complete legal protection also requires that it be possible for the unsuccessful tenderer to examine in sufficient time the validity of the award decision. Given the requirement that the Directive must have practical effect, a reasonable period must elapse between the time when the award decision is communicated to unsuccessful tenderers and the conclusion of the contract in order, in particular, to allow an application to be made for interim measures prior to the conclusion of the contract.[51]

The rationale behind the standstill period, as envisaged in the Remedies Directives, has been referred to by Treumer as allowing the economic operator adequate time to decide on whether to proceed with the review of the award decision or otherwise:

> The standstill period should give the tenderers concerned sufficient time to examine the contract award decision and to assess whether it is appropriate to initiate a review procedure, cf. consideration 6 of the Preamble to the Directive. This rule is based on a principle developed in the case law of the Court of Justice and is of utmost importance for the effective enforcement of the public procurement rules.[52]

Treumer continues to discuss whether:

> [A] similar principles apply for contracts outside of the scope of the Public Procurement Directives. This issue has not been considered in the case law of the Court of Justice but it has been addressed in national case law and in the legislation of at least a few Member States.

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51 Case C-212/02, *Commission v Austria*, [2004] ECLI:EU:C:2004:386, para. 23.

52 Steen Treumer and Francois Lichere (eds.), *Enforcement of the EU Public Procurement Rules*, (1st edn, DJOF Publishing Copenhagen 2011) 48.

> (…)
> It can be argued that a standstill period is also mandatory outside of the scope of the Public Procurement Directives. Individuals are entitled to effective judicial protection of the rights they derive from the Community legal order and the standstill period is a very important element in the creation of an effective remedies system.[53]

6 The Principle of 'Ineffectiveness'

Besides the introduction of effective standstill periods, the amending Directive 2007/66/EC has also introduced three instances when a public contract is deemed to be ineffective "by a review body independent of the contracting authority or that its ineffectiveness is the result of a decision of such review body".[54] The three instances of an ineffective contract as envisaged by the Directive are the following:

i. If the contracting authority has awarded a public contract without prior publication of a contract notice in the EU's Official Journal without this being permissible in accordance with Directive 200/18/EC;
ii. In cases where the tenderer has been deprived of resorting to review for pre-contractual remedies and
iii. "[I]n cases referred to in the second subparagraph of article 2b(c) of this Directive, if Member States have invoked the derogation from the standstill period for contracts based on a framework agreement and a dynamic purchasing system".[55]

The amending Directive 2007/66/EC further states that the consequences of a contract being considered ineffective shall be provided by national law.[56] Thus, while the Directive leaves much discretion to the Member States' domestic law, it proposes a number of non-mandatory remedies, such as that national law may provide for retroactive (*ex tunc*) cancellation of the contract or "limit the scope of the cancellation to those obligations which still have to be performed" (*ex nunc*).[57] Yet, Directive 2007/66/EC states that the Member States have to provide for other penalties in terms of article 2e(2), namely the imposition of fines on the contracting entity or the shortening of the public contract's

53 *Ibid.,* 48–49.
54 Directive 2007/66/EC, Article 2e.
55 *Ibid.*, Article 2d(1).
56 *Ibid.*, Article 2d(2).
57 *Ibid.*

duration. So, interestingly, Directive 2007/66/EC does not provide for both penalties to be raised simultaneously but for alternative mandatory penalties.

Directive 2007/66/EC leaves an exit clause for the Member States' independent review bodies, whereby they may not:

> consider a contract ineffective, even though it has been awarded illegally on the grounds mentioned in paragraph 1, if the review body finds, after having examined all relevant aspects, that overriding reasons relating to a general interest require that the effects of the contract should be maintained.[58]

However, Directive 2007/66/EC stops short of defining or describing these 'overriding reasons', thus leaving too much discretion on the Member States, who may also give a wide interpretation to the term, with negative implications for public procurement policy. Alternatively, Directive 2007/66/EC attempts to define 'overriding reasons' in such vague language, which in itself creates more legal uncertainty because, once again, Directive 2007/66/EC does not provide for a definition of what is deemed to be 'exceptional circumstances' and 'disproportionate consequences':

> Economic interests in the effectiveness of the contract may only be considered as overriding reasons if, in exceptional circumstances, ineffectiveness leads to disproportionate consequences.[59]

Directive 2007/66/EC stipulates what is not deemed to be an overriding interest, namely:

> However, economic interests directly linked to the contract concerned shall not constitute overriding reasons relating to a general interest. Economic interests directly linked to the contract include, *inter alia*, the costs resulting from the delay in the execution of the contract, the costs resulting from the launching of a new procurement procedure, the costs resulting from the change of the economic operator performing the contract and the costs of legal obligations resulting from the ineffectiveness.[60]

58 *Ibid.*, Article 2d(3).
59 *Ibid.*, Article 2d(3), para 2.
60 *Ibid.*, Article 2d(3), para 3.

The Maltese Public Procurement Regulations 2016 adopt the test of the examination of "all relevant aspects" in matters dealing with overriding reasons relating to a general interest, namely:

> The Public Contracts Review Board may not consider a contract ineffective, even though it has been awarded illegally, on the grounds mentioned in regulation 277, if the Public Contracts Review Board finds, after having examined all relevant aspects, that the overriding reasons relating to a general interest require that the effects of the contract shall be maintained.[61]

7 Overview of Council Directive 92/13/EEC of 25 February 1992 (Utilities)

Directive 92/13/EEC applies to remedies in the field of utilities, subject to a few exclusions.[62] This Directive provides for review procedures which are slightly different from those outlined in Directive 89/665/EEC and includes another ground, namely:

> measures other than those provided for in points (a) and (b) with the aim of correcting any identified infringement and preventing injury to the interests concerned; in particular making an order for the payment of a particular sum, in cases where the infringement has not been corrected or prevented.[63]

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61 Public Procurement Regulations 2016, Regulation 280(2).

62 *Ibid.*, Article 1 "This Directive applies to contracts referred to in Directive 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors (1), unless such contracts are excluded in accordance with art 5 (2), arts 18 to 26, arts 29 and 30 or art 62 of that Directive. Contracts within the meaning of this Directive include supply, works and service contracts, framework agreements and dynamic purchasing systems".

63 *Ibid.* Article 2(1) "The Member States shall ensure that the measures taken concerning the review procedures specified in art 1 include provision for the powers:

a. eitherto take, at the earliest opportunity and by way of interlocutory procedure, interim measures with the aim of correcting the alleged infringement or preventing further injury to the interests concerned, including measures to suspend or to ensure the suspension of the procedure for the award of a contract or the implementation of any decision taken by the contracting entity; and

This ground can be exercised instead of interim measures to set aside unlawful decisions. Directive 92/13/EEC provides that a contract cannot be concluded:

> before the expiry of a period of at least 10 calendar days with effect from the day following the date on which the contract award decision is sent to the tenderers and candidates concerned if fax or electronic means are used or, if other means of communication are used, before the expiry of a period of either at least 15 calendar days with effect from the day following the date on which the contract award decision is sent to the tenderers and candidates concerned or at least 10 calendar days with effect from the day following the date of the receipt of the contract award decision.[64]

This standstill period is provided to safeguard the tenderers'/candidates' right of appeal before a court of law, which has to meet the criteria established under Article 2(9) paragraph 2.[65] The Directive also provides an exhaustive list of derogations from the standstill period.[66] The grounds for the ineffectiveness of a public contract are the same grounds found in Directive 89/665/EEC.[67] The

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b. to set aside or ensure the setting aside of decisions taken unlawfully, including the removal of discriminatory technical, economic or financial specifications in the notice of contract, the periodic indicative notice, the notice on the existence of a system of qualification, the invitation to tender, the contract documents or in any other document relating to the contract award procedure in question;

or

c. to take, at the earliest opportunity, if possible by way of interlocutory procedures and if necessary by a final procedure on the substance, measures other than those provided for in points (a) and (b) with the aim of correcting any identified infringement and preventing injury to the interests concerned; in particular, making an order for the payment of a particular sum, in cases where the infringement has not been corrected or prevented.

Member States may take this choice either for all contracting entities or for categories of entities defined on the basis of objective criteria, in any event preserving the effectiveness of the measures laid down in order to prevent injury being caused to the interests concerned; and, in both the above cases, to award damages to persons injured by the infringement.

d. Where damages are claimed on the grounds that a decision has been taken unlawfully, Member States may, where their system of internal law so requires and provides bodies having the necessary powers for that purpose, provide that the contested decision must first be set aside or declared illegal".

64 Directive 92/13/EEC, Article 2a.

65 *Ibid.*, Article 2(9) para 2.

66 *Ibid.*, Article 2b.

67 *Ibid.*, Article 2d(1).

contents of Articles 2d and 2e of Directive 92/13/EEC are the same as Articles 2d and 2e of Directive 89/665/EEC.

The European Commission is empowered to notify the Member States before a contract is concluded and, if it deems that there is a serious infringement of European law on procurement, to notify the Member State concerned with the reasons for the infringement and solicit "its correction by appropriate means".[68] The Member State to whom the notification has been addressed has to inform the European Commission on whether the infringement has been corrected (or a reasoned submission[69] of why no correction has taken place) or that the notice of the contract award procedure has been suspended.[70]

8 Is There Space for Enhanced Harmonisation of the Remedies Directives Concerning Damages and Review Bodies to Achieve Effective Remedies?

The Treaty on the European Union emphasises the effective legal protection for all aspects of European Union law. The Treaty on European Union stipulates that "Member States shall provide remedies sufficient to ensure effective legal protection in the fields covered by Union law".[71] The Charter of Fundamental Rights of the European Union reiterates the right to effective remedies: 'Everyone whose rights and freedoms guaranteed by the law of the Union are violated the right to an effective remedy before a tribunal in compliance with the conditions laid down in this Article'.[72] In this respect, Craig and de Burca comment, "A robust line of cases in the early 1990s highlighted the tension between the emphasis on national procedural autonomy

68 *Ibid.*, Article 8(1) (2).

69 Directive 92/13/EEC, Article 8(4): "A reasoned submission communicated pursuant to paragraph 3(b) may rely among other matters on the fact that the alleged infringement is already the subject of judicial review proceedings or of a review as referred to in art 2(9). In such a case, the Member State shall inform the Commission of the result of those proceedings as soon as it becomes known".

70 Directive 92/13/EEC, Article 8(3): "Where notice has been given that a contract award procedure has been suspended in accordance with paragraph 3(c), the Member State concerned shall notify the Commission when the suspension is lifted or another contract procedure relating in whole or in part to the same subject matter is begun. That new notification shall confirm that the alleged infringement has been corrected or include a reasoned submission as to why no correction has been made".

71 Treaty on European Union, Article 19.

72 *Ibid.*, Article 47.

and the requirement that national remedies must secure the effectiveness of EU rights".[73] To this effect, two areas of the Remedies Directives have been identified where further harmonisation is needed. These are the harmonisation of the current review bodies and the heads of damages to be awarded by the same review bodies.

There is a need for this harmonisation and the consolidation of the three Remedies Directives into one directive to achieve more coherency, uniformity, legal certainty, and effectiveness. The current approach should emphasise effective, adequate judicial protection and the domestic courts' duty of sincere cooperation, namely that "the Union and the Member States shall, in full mutual respect, assist each other in carrying out tasks which flow from the Treaties".[74]

Member States have their legal traditions regarding what constitutes the heads of damages, and their review bodies are set up according to national law. With respect to damages, most Member States attribute heads of damages to be much wider and diversified than the damages outlined in the Remedies Directives. The same applies to review bodies, whereby each Member State has its own review bodies, which are constituted according to national law and with their peculiarities, reflecting the judicial autonomy of the Member States.

However, it is clear that the lack of harmonisation of review bodies and heads of damages, probably in part due to the judicial autonomy of the Member State, is another obstacle to the Internal Market because all economic operators in the field of public procurement expect that they are treated at a level playing field when their disputes reach the litigation stage.

Should some elements of the judicial autonomy be sacrificed to achieve more harmonisation in public procurement? The answer tilts towards the affirmative. Any proposals for a change in the Remedies Directives have to respect the principle of judicial autonomy and strike the right balance to find peaceful co-existence between the Member States' judicial autonomy and enhanced harmonisation in the field of effective remedies. There is a need for enhanced harmonisation to achieve more coherency, uniformity and legal certainty in the Member States' *corpus* of law. This position seems to tally with Craig and de Burca's views on national remedies for EU rights, who consider the current

73 Craig and de Burca (n 201) 269.

74 Treaty on European Union, Article 4(3). This article on sincere cooperation obliges the domestic courts' to give effective enforcement to EU law.

approach to be a balancing act between effective judicial protection and national procedural autonomy:

> it requires national courts to strike an appropriate, proportionality-based, case-by-case balance between the requirement of effective judicial protection for EU law rights and the application of legitimate national procedural and remedial rules. In deciding whether a national rule or principle could undermine the exercise of an EU law right, national courts must weigh the requirements of effectiveness and equivalence in the light of the aim and function of the national rule, bearing in mind also the importance and objective of the EU right in question.[75]

Remedies in public procurement are already available in the Member States. However, to have effective and rapid remedies, there is a need for more harmonisation of the Member States' domestic laws.

For instance, the following heads of damages should ideally be uniform across the Member States: *damnum emergens, lucrum cessans*, loss of chance, curricular damage and non-pecuniary damages. This is a proposed non-exhaustive list of damages the domestic court may accord. The Remedies Directives are silent on these heads of damages. Therefore, there is scope for harmonisation of the heads of damages, given that the Member States already provide heads of damages that go beyond the concept of damages in the Remedies Directives, albeit in different modes and forms. Furthermore, it is suggested that legal interest should commence from the date of conclusion of the public contract to the date when compensation in damages is paid. All this depends on the aggrieved party showing a valid bid and the nexus/causality between the injury/breach caused by the procurement process and the loss/damage suffered. Regarding the *quantum* of damages, this should ideally be left at the discretion of the national judge on a case-by-case basis because the *quantum* of damages has to be commensurate with the gravity of the infringement. Due consideration should be given to the proposal that the heads of damages should be harmonised across the Member States not to allow space for incoherent judgments.

During the *travaux preparatoire* on the draft Directive 89/665, at a point in time, three grounds of action for damages were proposed, namely the cost of unnecessary studies, forgone profits and lost opportunities. The final text of the Directive, however, is silent and refers only generally to the award of damages

75 Craig and de Burca (n 201) 277.

(Article 2(1)(c)). Concerns have been expressed that including forgone profits and lost opportunities could lead to speculative and wasteful litigation. However, these concepts of forgone profits and lost opportunities are finding their way into the Court of Justice of the European Union (CJEU) jurisprudence and the jurisprudence of the Member States.

There are two observations relating to damages litigation in public procurement. Firstly, business operators sometimes hesitate to bring a contracting authority before a court since they want to maintain good relations in the future. Litigation between a tenderer and a contracting authority often results in an irrevocable break in their relationship. Secondly, if damages are too generously and readily awarded, the contracting authority will carefully proceed to impede any public contract seriously.

Effective judicial protection can only be achieved if there is further harmonisation of the public procurement remedies in the Member States. This is not new for EU law because jurisprudence on damages in EU law is already elaborate and follows a consistent line of case law, namely when a right granted by the EU has been breached manifestly and seriously. If there is a link between the injury and the harm caused, liability in damages can be found.

So, one is not re-inventing the wheel when stating that there is scope for more harmonisation of damages to reach effectiveness. EU law on damages is already saturated, and what is needed is the importation of this *corpus* of law into the Remedies Directives while also capitalising on the Member States' legal/judicial practices. Therefore, the issue of judicial autonomy arises only to a certain extent. Article 2(1)(c) of the Public Sector Directive is too vague when it stipulates "award damages to persons harmed by an infringement"[76] without determining the heads of damages.

Given that the concept of damages should be better defined and harmonised in the Remedies Directives, it is suggested that Article 2(1)(c) of the Public Sector Directive should be amended to the effect that three elements have to subsist for a claim for damages to materialise, namely that the act of the contracting authority has to be unlawful thus resulting in a sufficiently serious breach of the rule of law intended to confer rights to individuals; the damage must be real, certain and quantifiable; and there should be the link between the conduct of the contracting authority and the damage caused to the injured bidder.

Given that the Remedies Directives are silent on pre-contractual damages, the Remedies Directives should consider the following heads of pre-contractual

76 Directive 2007/66/EC, Article 2(1)(c).

damages, namely the preparation costs for the submission of the tender, travel costs pertaining to the compilation of the tender, general business costs, legal/accountants' fees and other administrative expenses.

The Utilities Remedies Directive contains references to damages, but this does not augur well for legal certainty, uniformity and coherency concerning effective remedies. The references to damages in the Utilities Remedies Directive are more elaborate than the references to damages in the Public Sector Remedies Directive. This supports the view that there is a need not only for harmonisation of the heads of damages but also for harmonisation of damages in the Remedies Directives, possibly by consolidating the three Remedies Directives into one Directive, or better, a Regulation.

Short of this, there should be a common clause in the Public Sector Remedies Directive and the Utilities Remedies Directive that defines what constitutes precontractual damages and post-award damages; this proposal, although elaborate, is not exhaustive (to allow space for judicial autonomy). It is also proposed that the *quantum* of damages should be left to the discretion of the Member States' domestic courts and that the aggrieved bidder should provide the proof.

Concerning review bodies, the Public Sector Remedies Directive puts the onus on the Member States to take the necessary measures to ensure that the decisions taken by the contracting authorities can be reviewed effectively, adequately and as rapidly as possible. However, the Remedies Directives fail to prescribe the form and type of forum capable of pronouncing effective, adequate and rapid remedies.

The Public Sector Remedies Directive simply emphasises that the body of the first instance should be independent of the contracting authority and that the decisions of the review body should be effectively enforced. However, the form is left within the discretion of the Member States. Moreover, this issue of effective enforcement has been questioned, given that each Member State has its peculiar enforcement measures. This means that through this lack of harmonisation, discrimination and legal uncertainty may arise because of the legal incoherency.

Article 2(9) of the Public Sector Remedies Directive refers also to review bodies that are not judicial, in which case these bodies have to provide "written reasons for their decisions".[77] To remedy this situation, it is proposed that these review bodies, for effectiveness, uniformity and legal certainty, should always be judicial in character and not quasi-judicial. Review bodies at first instance, whether established under civil law or administrative law, should comprise

77 *Ibid.*, Article 2(9).

at least two lawyers well-versed in public procurement law, with one acting as chairman and another knowledgeable and technical member concerning public procurement law and policy. Therefore, the Public Sector Remedies Directive should, at a minimum, prescribe the composition of the review body in the first instance.

Article 2(9) of the Public Sector Remedies Directive adds that the first instance review body decisions have to be judicially reviewed "by another body which is a court or tribunal within the meaning of Article 234 of the Treaty and independent of both the contracting authority and the review body".[78] However, this again does not provide an adequate safeguard because if the review body of the first instance is not properly constituted, especially in cases of quasi-judicial bodies, the review body at the second instance will be hampered in the sense that the second instance review body can only review the case on points of law. Therefore, if the review body in the first instance has not properly grasped the points of fact, the aggrieved party will be prejudiced because, in the second instance appeal, he can only raise points of law. Thus, it has been proved that there is a need for enhanced harmonisation of first instance review bodies, as the lack of harmonisation of first instance review bodies may result in ineffective remedies for the aggrieved bidder.

The Remedies Directives are presently devoid of rules on review bodies' form, competence and jurisdiction. It is thus appropriate to remedy these lacunae by prescribing the form, competence and jurisdiction of review bodies in the Member States while still respecting the power of the domestic legal systems of the Member States to designate their judicial bodies. Therefore, it is recommended that where the review body is not judicial, any appeal from a decision of the review body should be not only on points of law but also on points of fact. The Directives should also specify that the second instance body of review should be the Court of Appeal as properly constituted by the domestic laws of the respective Member States.

It appears that the Remedies Directives with respect to review bodies and damages do indeed lack the necessary safeguards to achieve uniformity, legal certainty and effectiveness. Thus, there is a dire need for more harmonisation of these two areas of law. There is also a need to consolidate the Remedies Directives, in the sense that the provisions on review bodies and the heads of damages should be similar in both directives, whether for the public or utility sectors.

Suppose damages and review bodies remain unregulated at an EU law level. In that case, the general principles of legal certainty, non-discrimination and

78 *Ibid.*

legitimate expectations, which rank among the higher norms of EU law, will continue to be jeopardised. Therefore, there is space for the judicial autonomy of the Member States to be curtailed or for the right balance to be achieved between EU law and judicial autonomy to give effect to higher norms of EU law, namely the achievement of truly effective remedies in public procurement.

9 Conclusion

There is certainly a need for more harmonisation of the review bodies and heads of damages because divergent domestic laws may result in ineffective and incoherent application of EU law, what Koen Lenaerts, President of the Court of Justice, refers to as affecting the primacy and direct effect of EU law. One cannot any longer hide behind the veil of judicial autonomy. Some aspects of the Remedies Directives need immediate harmonisation for legal certainty and EU law's full, direct, uniform effect in the Member States. The divergent legal norms in the Member States prove that without the much-needed harmonisation of public procurement remedies, there is no effective legal protection for aggrieved tenderers. While one speaks of legal certainty, one rarely speaks of judicial certainty. For judicial certainty to be achieved, there has to be enhanced harmonisation of the review bodies and enhanced harmonisation of the damages awarded by these review bodies.

Enhanced harmonisation of these aspects does not necessarily militate against the principle of judicial autonomy. Rather, one can speak of judicial autonomy with an underlying base of judicial certainty. There can be no proper judicial autonomy if the prerequisite of judicial certainty is lacking. Thus, review bodies have to have permanence, compulsory jurisdiction, apply uniform rules of law, and they should be characterised by independence, impartiality and security of tenure while applying in their awards heads of damages that are uniform across the Member States, albeit for the *quantum* that has to be decided on a case-by-case basis. As it stands now, each Member State has its own domestic rules, and thus, there is a need for further harmonisation of the heads of damages and review bodies.

It has also been evident that the minimum harmonisation measures offered by the Remedies Directives jeopardise the safeguards of effective remedies, leading to legal/judicial barriers to accessing effective and rapid remedies in the Internal Market. With the current lack of uniformity, legal and judicial certainty are jeopardised, with the ultimate effect being the inadequate significance of the effectiveness of the judicial remedy sought by the aggrieved bidder.

Therefore, enhanced judicial protection in public procurement, being an increasingly important economic sector, can contribute to the completion of

the internal market by ensuring fair and free competition, the reduction of public expenditures through lower priced and quality goods, better and more efficient application of the public procurement directives, including the Remedies Directives, which in turn will result in better services to the consumer, better value for money for the contracting authorities, more efficient use of taxpayers' money thus fighting endemic corruption and protectionism in the award of public contracts. It can also improve productivity and cross-border trade within the Internal Market and with third countries. Furthermore, open and non-discriminatory public procurement contributes to the competitiveness of EU economic operators.

Another hurdle is that the EU must ensure reciprocal public procurement access with its trading partners. This non-reciprocity is a source of unfair competition in public procurement in the Internal Market. The EU should ensure greater market access in third countries based on reciprocity, and the EU's trading partners should not reciprocate the EU's open access with protectionism from their side. The EU should push its trading partners to sign the World Trade Organisation's Government Procurement Agreement and remove any reservations. The EU should also be more vigilant on advantageous bids from third countries' economic operators, where bids are supported by state aid, dumping practices, state guarantees, infringement of property rights, and human rights violations, especially concerning general labour law and, in particular child labour, disrespect for environmental standards and non-conformity with major international conventions. These practices are neither free nor fair trade and should be rejected because they are the antithesis of the rules of the Internal Market.

The EU should increase its leverage with its trading partners in its negotiations of international trade agreements and deep and comprehensive trade agreements so that the EU's trading partners can open their procurement markets, based on reciprocity, to economic operators from the EU. Only in this way can one ensure that international trade in public procurement flows freely and fairly, thus reaping benefits for economic operators and consumers alike, with the added benefit of achieving value for money for taxpayers.

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CHAPTER 11

Data Retention: an Internal Market or a Criminal Law Matter?

Oleksandr Pastukhov

Abstract

This paper addresses the problem of adopting EU measures on criminal law matters based on Article 114 TFEU (former Article 95 TEC), which confers on the EU a competence to adopt measures aimed at the approximation of the Member States' laws and regulations for purposes of "the establishment and functioning of the Internal Market". Using EU data retention legislation as an example, the piece demonstrates that the EU legislators are using market-making as a pretext for adopting legal harmonisation measures in numerous areas which are otherwise off-limits to EU harmonisation efforts, and the Court of Justice of the European Union is exceedingly lenient in upholding such measures. The piece argues that the choice of Article 114 as a legal basis for legal harmonisation results in the EU's 'competence creep' that, given the Court's position, can only be stopped by amending the text of the Article.

1 What Is Data Retention?

Many of our routine daily activities, such as shopping, taking a bus or talking over the phone, leave a 'paper trail': receipts, tickets, invoices, etc. This is because the vendors and service providers are legally obligated to retain the documents related to the corresponding transactions for tax reporting purposes. Moreover, companies have their reasons for retaining data on their customers and their dealings: bookkeeping, billing, customer service, quality assurance, and other business purposes. Finally, the data can be retained in the hope that it can be later sold to advertisers, marketers, and other industries.

The 'paper trail' is increasingly becoming a 'digital imprint'. The processing power of modern computers makes possible, on one hand, mass surveillance and, on the other, singling out individuals and creating their detailed profiles.

The legislators have long realised the threats of unlimited data retention. As early as 1973, when the Council of Europe first took up the issue of personal data retention, it suggested in its Committee of Minister's Resolution that

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personal data users were under an obligation to erase "obsolete data". However, in the Explanatory Report on the same Resolution, the Committee denied recognition of a formal "right of oblivion". It claimed it sought to protect individuals from "unreasonably long retention of data that could be harmful".[1] Nevertheless, the Resolution prescribed no specific periods or guidelines on their setting. It merely called for rules to be "laid down to specify the periods beyond which certain categories of information should no longer be kept or used".[2]

In 1974, the Council of Europe explicitly recognised data subjects' "legitimate interest in seeing certain kinds of information concerning them, particularly that which is harmful to them, wiped off or rendered inoperative after a certain time has passed".[3] In 1981, the same international organisation acknowledged the situation with medical databanks as a "threat to privacy if information relating to any individual is allowed to accumulate as the years go by".[4]

The work of the Council of Europe on personal data protection culminated the same year with the adoption of the Convention on Data Protection[5] that prescribed rules for the "automatic processing" of personal data, including automated storage, computer processing, alteration, erasure, retrieval and dissemination of data, both in the public and the private sectors. The Convention allows personal data to be "preserved in a form which permits identification of the data subjects for no longer than is required for the purpose for which those data are stored".[6]

It followed from the Convention's data retention rule that data that were not preserved in a form making the identification of data subjects possible could be retained longer than needed to store the data. According to the Explanatory

1 Council of Europe, Committee of Ministers, Resolution (73) 22 on the protection of the privacy of individuals *vis-à-vis* electronic data banks in the private sector (Adopted by the Committee of Ministers on 26 September 1973 at the 224th meeting of the Ministers' Deputies), Explanatory Report, para 24, available at <https://rm.coe.int/16805028 30> accessed 20 April 2024.

2 *Ibid*., Annex, para 4.

3 Council of Europe, Committee of Ministers, Resolution (74) 29 on the protection of the privacy of individuals *vis-à-vis* electronic data banks in the public sector (Adopted by the Committee of Ministers on 20 September 1974 at the 236th meeting of the Ministers' Deputies), para 21, available at <https://rm.coe.int/09000016807aa909> accessed 20 April 2024.

4 Council of Europe, Committee of Ministers, Explanatory Memorandum to Recommendation No. R (81) 1 on regulations for automated medical banks (Strasbourg 1981), para. 52, available at <http://www.ipst.pt/files/IPST/LEGISLACAO/Legislacao_Comunitaria/Rec_1981-1.pdf> accessed 20 April 2024.

5 Convention for the Protection of Individuals with regard to Automatic Processing of Personal Data. Strasbourg, 28.I.1981.

6 *Ibid*., art 5(e).

Report on the Convention prepared by the Committee of Ministers, this did not mean that "data should after some time be irrevocably separated from the name of the person to whom they relate" but rather that "it should not be possible to link the data and the identifiers readily".[7]

The 1989 UN Guidelines for the Regulation of Computerised Personal Data Files recommend that "[t]he period for which the personal data are kept does not exceed that which would enable the achievement of the purposes [...] specified".[8] Data retention is of secondary importance in the quoted provision, the primary one being attached to the notification of data subjects to collect personal data.

The 1980 OECD Privacy Guidelines are even less explicit, providing that "[t]he purposes for which personal data are collected should be specified not later than at the time of data collection and the subsequent use limited to the fulfilment of those purposes or such others as are not incompatible with those purposes and as are specified on each occasion of change of purpose".[9] The data subject's right to have the data erased is envisaged in the OECD Guidelines as a result of a successful challenge of the data, but the grounds for the challenge are not specified.[10]

Still, the decade that followed the adoption of the Council of Europe Convention contributed significantly to establishing in the minds of law- and policy-makers a clear link between the purpose of processing personal data and the period during which the data were allowed to be retained. It also became evident in the 1980s that concrete terms of retention had to be fixed for different types of data and data users. Thus, a 1985 Recommendation of the Council of Europe called for establishing different retention periods for different categories of data and each kind of social benefit.[11]

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7 Council of Europe, Committee of Ministers, Explanatory Report on the Convention for the Protection of Individuals with regard to Automatic Processing of Personal Data, Texts Adopted, ETS No. 108 (1981), para 42, available at <http://conventions.coe.int/Treaty/en/Reports/Html/108.htm> accessed 20 April 2024.

8 Guidelines for the Regulation of Computerized Personal Data Files, GA Res. 44/132, UN GAOR, 44th Sess., Supp. No. 49, UN Doc. A/44/49 (1989), 211, available at http://www1.umn.edu/humanrts/instree/q2grcpd.htm accessed 20 April 2024.

9 OECD Guidelines on the Protection of Privacy and Transborder Flows of Personal Data (1980), para 9, available at <http://www.oecd.org/document/18/0,3343,en_2649_34255_1815186_1_1_1_1,00.html> accessed 20 April 2024.

10 *Ibid.*, para. 13(d).

11 Council of Europe, Committee of Ministers, Recommendation No. R (86) 1 of the Committee of Ministers to Member States on the Protection of Personal Data used for Social Security Purposes, Texts Adopted (1986), available at <https://rm.coe.int/cmrec-86-1-on

Unfortunately, the retention periods have not been capped for any kind of data neither by the 1995 Data Protection Directive nor by the General Data Protection Regulation (GDPR)[12] that replaced it in 2018. Nevertheless, as regards one particular type of personal data – communications data – the story is much more complicated.

2 What Is Communications Data Retention?

If any of us some thirty years ago had been told that in thirty years, most people, from children to seniors, would – voluntarily! – be carrying on them personal tracking devices akin to ankle monitors (tethers) used in law enforcement, no one would have believed it. However, this is exactly what is happening now, in the year 2024, for the cell phones we have become so dependent on act exactly like those tracking bracelets: they periodically emit radio signals that, after being interpreted, inform the mobile phone company of the device's – and hence the user's – location. The location data thus generated and traffic data, such as numbers dialled or called from, are being collected and processed by the provider for reporting and operational purposes (billing, customer service, quality assurance, etc.). With data mining methods, these data can be assembled into detailed personality profiles, including contacts, travels, shopping habits, and political, religious and sexual likes and dislikes, for all users of electronic communication services, that is, almost the entire population.

In 1995, the Council of Europe recommended that:

> [d]ata needed for billing should not be stored by network operators or network providers for a period which is longer than strictly necessary for settling the account, bearing in mind the possible need to store data for a reasonable period with a view to complaints on the billing, or if legal provisions require those data to be kept longer.[13]

-the-protection-of-personal-data-used-for-social-security/1680a43b57> accessed 20 April 2024.

12 Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation) [2016] OJ L 119/1.

13 Council of Europe, Committee of Ministers, Recommendation No. R (95) 4 of the Committee of Ministers to Member States on the protection of personal data in the area of telecommunication services, with particular reference to telephone services (Adopted by the Committee of Ministers on 7 February 1995 at the 528th meeting of the Ministers'

For example, a legal requirement of data retention for a period longer than necessary for billing purposes may exist for law enforcement reasons. However, even in that case, "the law should be explicit about the duration of storage of criminal intelligence", and excessively long retention periods are not justified "simply because you never know whether any data 'might perhaps come in handy in any unforeseeable future'".[14]

In the EU, the issue of the retention of communications data was first addressed by the 'data retention amendment' to the so-called e-Privacy Directive, whereby the Member States were allowed to "adopt legislative measures providing for the retention of data for a limited period justified on the grounds" of "national security (i.e. State security), defence, public security, and the prevention, investigation, detection and prosecution of criminal offences or of unauthorised use of the electronic communication system".[15]

The 'data retention amendment' was adopted in 2002 under the influence of 9/11. Soon after, a special Council's Framework Decision was drafted secretly, but Statewatch leaked the text.[16] According to it, communications data obtained in the way described above were to be retained by the operators for 12–24 months, a period much longer than they needed or, in fact, wanted.

A revised draft Framework Decision on the mandatory retention of the data resulting from electronic communications was sent to the European Parliament in late April 2004[17] following the Madrid train bombings a month earlier. This started the public part of the law-making process. Instead of an obligation to store traffic data already processed by companies for billing or

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Deputies), available at <https://rm.coe.int/CoERMPublicCommonSearchServices/DisplayDCTMContent?documentId=0900001680501o8e> accessed 20 April 2024.

14 Second Evaluation of the Relevance of Recommendation No. R (87) 15 Regulating the Use of Personal Data in the Police Sector, Done in 1998 (1999), App. D, s 5.2.3., available at <http://www.coe.int/t/dghl/standardsetting/dataprotection/EM/2Evaluation(87)15_EN.pdf> accessed 20 April 2024.

15 Directive 2002/58/EC of the European Parliament and of the Council of 12 July 2002 concerning the processing of personal data and the protection of privacy in the electronic communications sector (Directive on privacy and electronic communications) [2002] OJ L 201/37, art. 15(1).

16 See Statewatch, Statewatch News online: Draft EU Framework Decision on data retention, 2 March 2012, <https://www.statewatch.org/news/2002/august/statewatch-news-online-draft-eu-framework-decision-on-data-retention/> accessed 20 April 2024.

17 Council of the European Union, Draft Framework Decision on the retention of data processed and stored in connection with the provision of publicly available electronic communications services or data on public communications networks for the purpose of prevention, investigation, detection and prosecution of crime and criminal offences including terrorism (8958/04), available at <https://db.eurocrim.org/db/en/doc/417.pdf> accessed 20 April 2024.

other internal purposes, a majority in the Council was now in favour of an obligation to collect and store all communications data for law enforcement purposes. This included, for example, the location data collected when using a mobile phone, the history of websites visited, IP numbers of parties contacted via instant messaging services, as well as addresses and senders of all e-mails sent and received. These data would have to be collected by Internet service providers (ISPs) and telecom companies, but standardised interfaces would facilitate access for law enforcement and intelligence services.

The last version of the draft Framework Decision increased the maximum retention term to 36 months. It also named as a reason for the retention the "prevention, investigation, detection and prosecution of crime and criminal offences".[18] This would result in the use of the retained data being authorised even in the case of minor offences.

Under the EU's former three-pillar system, harmonising law enforcement rules was part of the Third Pillar. The European Parliament had to be only formally consulted about the proposal and could not veto or change it. As the Council's data retention scheme implied an obligation of private actors – ISPs and telecom companies – to store the data, it was questionable from the very beginning whether the measure did not touch upon the First Pillar issues and thus had to be adopted under the co-decision procedure where the European Parliament has much more of a say. When the e-Privacy Directive was debated in the Parliament, many MEPs had already opposed adopting Article 15, which allowed Member States to introduce national laws on data retention, since it introduced Third Pillar issues into a First Pillar instrument. The Parliament rejected the proposed Framework Decision on 27 September 2005,[19] citing concerns over the legal basis chosen, the proportionality of the measure and the incompatibility with Article 8 of the European Convention on Human Rights.[20]

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18 See *ibid.*

19 See European Parliament legislative resolution on the initiative by the French Republic, Ireland, the Kingdom of Sweden and the United Kingdom for a Draft Framework Decision on the retention of data processed and stored in connection with the provision of publicly available electronic communications services or data on public communications networks for the purpose of prevention, investigation, detection and prosecution of crime and criminal offences including terrorism (P6_TA(2005)0348), available at <https://www.europarl.europa.eu/doceo/document/TA-6-2005-0348_EN.html> accessed 20 April 2024.

20 See European Parliament, Report on the initiative by the French Republic, Ireland, the Kingdom of Sweden and the United Kingdom for a Draft Framework Decision on the retention of data processed and stored in connection with the provision of publicly

The European Commission, despite previously opposing the idea of communications data retention, redrafted the proposal as a Directive. In the wake of the July 2005 London metro bombings, the UK government argued that the measure would help fight terrorism and other serious crimes. The Blair cabinet used the UK presidency in the Council to impose a deadline of the end of 2005 for the European Parliament to agree the text, which the Parliament did on 14 December 2005 following a single reading. The Council adopted the measure by a qualified majority, with Ireland and Slovakia voting against it, and the Directive was passed into law in March 2006.

As a derogation from the rules of the e-Privacy Directive allowed by its Article 15, Directive 2006/24/EC, commonly known as the Data Retention Directive, required data on communications traffic (data on the origin, destination, type and time of the communication), equipment used (telephone numbers, IMSI and IMEI codes) and its location (cell IDs and data identifying the cells' geographical location) – not the content of the communications – to be retained by "providers of publicly available electronic communications services or of a public communications network".[21] As a result, despite numerous counter-arguments put forward by human rights activists, privacy advocates, the industry and academia, mandatory communications data retention terms ranging from 6 to 24 months were established throughout the EU.

Such an EU-wide blanket data retention arrangement set by the Directive involves additional costs for the providers who pass them on to their clients. This results in consumers, mostly law-abiding taxpayers, being charged for being spied on. The compensation to the providers for the costs incurred is very low or absent, depending on the country. This makes the extended retention particularly burdensome for SMEs, which are plenty among ISPs, distorts competition within the Internal Market and puts the whole EU ICT industry in a disadvantaged position in the global marketplace.

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available electronic communications services or data on public communications networks for the purpose of prevention, investigation, detection and prosecution of crime and criminal offences including terrorism (A6-0174/2005), available at <https://www.europarl.europa.eu/doceo/document/A-6-2005-0174_EN.html?redirect> accessed 20 April 2024.

21 Directive 2006/24/EC of the European Parliament and of the Council of 15 March 2006 on the retention of data generated or processed in connection with the provision of publicly available electronic communications services or of public communications networks and amending Directive 2002/58/EC [2006] OJ L 105/54, arts 1, 5.

3 What Is the Appropriate Legal Basis?

Ireland, one of the two countries that voted against Directive 2006/24/EC in the Council, brought an action for annulment before the ECJ on the ground that the measure was not adopted on an appropriate legal basis (Article 95 TEC, now Article 114 TFEU).[22] The applicant was supported by Slovakia, the other country that voted against the Directive in the Council. The Commission, the European Data Protection Supervisor, Spain, and the Netherlands supported the defendants, the Parliament and the Council.

Ireland argued that the sole or principal objective, the 'centre of gravity' of the Directive, was investigating, detecting and prosecuting crime and not establishing or functioning of the Internal Market. Article 95(1) conferred on the EU a competence to "adopt the measures for the approximation of the provisions laid down by law, regulation or administrative action in the Member States which have as their object the establishment and functioning of the Internal Market". Article 95 of the TEC, now Article 114 of the TFEU, can be used where disparities exist (or are likely to exist in the future) between national rules which obstruct fundamental freedoms or create distortions of competition and thus directly affect the functioning of the Internal Market.[23]

The Court rejected the applicant's view. The Court agreed with the defendants, who claimed that the directive's premise was to harmonise disparities between national provisions governing data retention by service providers, particularly regarding the nature of data retained and periods of data retention. It was apparent to the Court that differences were liable to directly impact the functioning of the Internal Market, which would become more serious over time.[24]

Moreover, the Court has noted that Article 47 of the EU Treaty provides that none of the provisions of the EC Treaty may be affected by a provision of the EU Treaty to safeguard the building of the *acquis communautaire*. Insofar as Directive 2006/24 comes within the scope of Community powers, it could not be based on a provision of the EU Treaty without infringing Article 47. The provisions of Directive 2006/24 are limited to the activities of service providers and do not govern access to data or use thereof by police or judicial authorities

22 Case C-301/06 *Ireland v European Parliament and Council of the European Union* [2009] ECR I-593.

23 See, e.g., Case C-376/98 *Germany v. Parliament and Council* [2000] ECR I-8419; Case C-210/03 *Swedish Match* [2004] ECR I-11893; Case C-380/03 *Germany v Parliament* [2006] ECR I-11573.

24 See *Ireland v European Parliament and Council of the European Union* (n 23) paras 62–71.

of the Member States. The said provisions are designed to harmonise national laws on the obligation to retain data, the categories of data to be retained, the periods of data retention, data protection and security, and the conditions for data storage. The measure does not involve intervention by police or law enforcement authorities of the Member States, nor access, use or exchange by them. Thus, according to the Court, Directive 2006/24 relates predominantly to the functioning of the Internal Market.[25]

It is shocking to see the levels of formalism, legalism and legal positivism the Court has demonstrated when deciding the case, how easily it ignores the measure's legislative history (let alone the story of the failed Framework Decision and the UK's twisting arms of the MEPs) and the obvious hidden agenda of mass surveillance behind it. "[T]he Court's inquiry has a weary feel and scarcely extends beyond the perfunctory".[26] Moreover, the Court takes sides:

> It draws on the evidence of those directly and partially implicated in the adoption of the measure in the first place – the Commission, the Council and States who had voted in favour of the measure in the Council, the Parliament, and the European Data Protection Supervisor. The Court skips lightly over the legal threshold and the factual appraisal: the Directive is valid.[27]

To some experts in EU law, the decision came as a big surprise:

> The judgment in *Ireland v Parliament and Council* would have provided good odds at an EC constitutional betting forum. Indeed, few would have thought that the internal market provision of Art 114 TFEU was capable of regulating the fight against terrorism and organised crime in the context of data retention.[28]

The surprise was even bigger for those who were familiar with the earlier case of *Parliament v. Council,* whereby the Court annulled a Council Decision (2004/496) on the conclusion of an agreement between the EC and the United States on the processing and transfer of passenger name record (PNR) data by

25 See *ibid.* paras 75, 78, 80–83.

26 Stephen Weatherill, 'The Limits of Legislative Harmonization Ten Years after Tobacco Advertising: How the Court's Case Law has become a "Drafting Guide"' (2011) 12(3) German Law Journal 827, 840.

27 *Ibid.*

28 Ester Herlin-Karnell, 'Annotation, Case Comment Case C-301/06, Ireland v. Parliament and Council' (2009) 46 Common Market Law Review 1667.

air carriers to the U.S. authorities.[29] *Parliament v. Council* is a rare example of the Court refusing to accept legislative reliance on Article 95 TEC, now Article 114 TFEU.[30] The Council Decision was based on a parent Directive (95/46), which, in turn, was based on Article 100a (subsequently Article 95 TEC). "The Court once again did not investigate beyond the recitals"[31] but found that although private operators have collected the PNR data for commercial purposes and it is they who arrange for their transfer to a third country, the transfer in question [...] falls within a framework established by the public authorities that relate to public security.[32]

It is as if ISPs and telecom operators were obligated to retain data for themselves and not to transfer them "within a framework established by the public authorities that relates to public security"! Article 8 of the Data Retention Directive reads:

> Member States shall ensure that the data specified in Article 5 are retained in accordance with this Directive in such a way that the data retained and any other necessary information relating to such data can be transmitted upon request to the competent authorities without undue delay.

The Court's judgement in *Ireland v Parliament and Council* is also difficult to align with the later *Digital Rights Ireland* decision by which the same Court annulled Directive 2006/24 on human rights grounds.[33] In the latter case, the Court has established that "The material objective of that directive is [...] to contribute to the fight against serious crime and thus, ultimately, to public security".[34]

4 Why Does the Legal Basis Matter?

The choice of a legal basis for an EU measure is not a scholastic issue but one that has far-reaching practical implications. As illustrated by the case of communications data retention legislation above, the process of adopting an EU instrument and, thus, the process of reaching a societal consensus (lobbying,

29 See Cases C-317/04 & C-318/04 *Parliament v Council* [2006] ECR I-4721.

30 "So the limits of Article 114 TFEU are glimpsed. But this is rare". Weatherill (n 26) 841.

31 *Ibid.*

32 *Parliament v. Council* (n 29) para 58.

33 See Joined cases C-293/12 and C-594/12 *Digital Rights Ireland and Seitlinger and others v Minister for Communications, Marine and Natural Resources and others* [2014] ECR I-238.

34 *Ibid.*, para. 41.

forming alliances, horse-trading, etc.) on the issue addressed by the instrument are significantly different when different legal bases are chosen.

Since the entry into force of the Lisbon Treaty in 2009, AFSJ (Area of Freedom, Security and Justice, former Third Pillar) measures have been subject to the ordinary legislative procedure, with some exceptions. These include measures intended to ensure "administrative cooperation between the relevant departments of the Member States" (Article 74 of the TFEU), which are still subject to the special legislative procedure with the Council acting on a proposal of the Commission or a quarter of the Member States, and after consulting the Parliament. The special legislative procedure also applies to measures laying down the conditions and limitations for police cooperation (Article 89 of the TFEU) and provisions on passports, identity cards and residence permits (Article 77(3) of the TFEU). Moreover, in the AFSJ 'track', Ireland and Denmark enjoy the right to opt-out from an EU measure. Finally, a measure adopted under Article 114 of the TFEU can be a directly applicable regulation, which is not an option under the AFSJ rules.

At the same time, an Internal Market-related harmonisation measure can be adopted by a qualified majority in the Council and a simple majority in the Parliament. The threshold for adopting a measure under Article 114 of the TFEU is shockingly low: all the legislator has to do is to use the language adopted by the Court in the Article 100a/95/114 cases. No scientific evidence is required to demonstrate the existence of trade barriers or distortions to the Internal Market. Whatever is stated in the preamble is taken for granted. The same applies to the principles of subsidiarity and proportionality: they have become a mere box to tick in the recitals.[35] Even when the text is far from perfect in terms of emulating the Court's language (e.g., Article 8 of Directive 2001/37), the Court generously rubberstamps instruments that, according to the legislator, contribute to the functioning of the Internal Market.[36] As a result, since – with creative drafting – any area of human activities can be presented as related to the establishment or functioning of the Internal Market, anything under the sun can become the subject of the EU's legal harmonisation.

35 All is needed is the following statement: "Since the objective of this [measure], namely to [...], cannot be sufficiently achieved by Member States but can rather, by reason of its scale and effects, be better achieved at Union level, the Union may adopt measures in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty on European Union. In accordance with the principle of proportionality, as set out in that Article, this [measure] does not go beyond what is necessary in order to achieve that objective". Recital 36 of Directive (EU) 2016/943, Recital 170 of the GDPR, Recital 176 of the Artificial Intelligence Act and countless others.

36 See, e.g., Case C-210/03 *Swedish Match* [2004] ECR I-11893.

> This is the true energy of Article 114. The EU legislature need not seek to disguise the re-regulatory dimension of its harmonisation initiatives. It needs only to tie that re-regulatory dimension sufficiently tightly to the market-making function of harmonisation. However, that is not difficult to achieve, partly because the Court is generous in its interpretation of the scope of the legislative grant but mainly because the Treaty, and the concept of the Internal Market in particular, is simply broad.[37]

The vague language of Article 95 has led to the adoption of numerous EU measures in the name of market-making in many areas in which the EU's competencies are limited (e.g., criminal law, environmental law, consumer protection, protection and improvement of human health, culture)[38] or in which harmonisation of laws is explicitly prohibited (e.g., public health).[39] This, in turn, leads to the so-called 'competence creep' – the ever-expanding "limits of the competencies conferred" upon the EU by the Member States, as envisaged by Article 5 of the TEU.

As for criminal law matters generally, the ease of adopting a measure under Article 114 of the TFEU, even against the will of some Member States, the lenient position of the Court[40] and the resulting 'competence creep' mean more 'Europeanisation' of the criminal law of the Member States and more 'federalisation' of the EU. Whether these are the desired outcomes depends on personal views of the ultimate goal of the very EU project and remains highly contested.[41]

As for data retention matters specifically, the Internal Market 'track' is set to produce more and more EU rules on data retention for law enforcement purposes in various fields. The EU anti-money laundering (AML) legislation provides an excellent example of this trend. Whereas the so-called 3rd AML Directive of 2005 required financial institutions and other relevant persons to keep "documents and information" related to "customer due diligence", "business relationships and transactions" "for use in any investigation into, or

37 Weatherill (n 26) 834.

38 See Sybe A. de Vries, *Tensions within in the Internal Market: The functioning of the Internal Market and the Development of Horizontal and Flanking Policies* (Europa Law Publishing 2006) 274–297.

39 See art 168(5) TFEU.

40 A more recent example of the Court's upholding a directive on a criminal law matter adopted under art 114 TFEU is *Czech Republic v European Parliament and Council of the European Union*. This action for annulment challenged the validity of Directive (EU) 2017/853 of the European Parliament and of the Council of 17 May 2017 amending Council Directive 91/477/EEC on control of the acquisition and possession of weapons.

41 See Jacob Olav Göran Öberg, 'The Legal Basis for EU Criminal Law Harmonisation: A Question of Federalism?' (2018) 43(3) European Law Review 366.

analysis of, possible money laundering or terrorist financing by the FIU or by other competent authorities in accordance with national law" "for a period of a period of at least five years following the carrying-out of the transactions or the end of the business relationship",[42] the so-called 4th AML Directive of 2015 gives the Member States the right to:

> allow or require further retention after they have carried out a thorough assessment of the necessity and proportionality of such further retention and consider it to be justified as necessary for the prevention, detection or investigation of money laundering or terrorist financing. That further retention period shall not exceed five additional years.[43]

However, this is not the end of the story. The so-called 5th AML Directive of 2018 reformulates the rule of Article 40(1)(a) of the 4th AML Directive as follows:

> in the case of customer due diligence, a copy of the documents and information which are necessary to comply with the customer due diligence requirements laid down in Chapter II, including, where available, information obtained through electronic identification means, relevant trust services as set out in Regulation (EU) No 910/2014 or any other secure, remote or electronic, identification process regulated, recognised, approved or accepted by the relevant national authorities, for a period of five years after the end of the business relationship with their customer or after the date of an occasional transaction;

and adds to it a new paragraph:

> The retention period referred to in this paragraph, including the further retention period that shall not exceed five additional years, shall also apply in respect of the data accessible through the centralised mechanisms referred to in Article 32a.

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42 Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing [2005] OJ L 309/15, art 30.

43 Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC [2015] OJ L 141/73, art 40(1).

Not surprisingly, the legal basis of all the three AML directives mentioned above is Article 95 of the TEC or Article 114 of the TFEU. As one can see, the hunger of the law enforcement authorities for more personal financial data is matched only by the EU's hunger for more competencies. However, whereas the earlier justify their appetite by needing the data for "the prevention, detection or investigation of money laundering or terrorist financing", the latter keeps adopting legal instruments clearly aimed to serve law enforcement purposes, justifying them by reasons pertaining to "the establishment and functioning of the Internal Market".

5 What to Do about the Resulting 'Competence Creep'?

Of course, it is up to EU citizens to decide if they want to live in a 'database state'. Many eagerly trade away freedom for security. However, the EU's never-ending legal harmonisation bonanza under the market-making pretext must be stopped. The peoples of Europe gave the EU a mandate to regulate the Internal Market, not to use it as an excuse for power grabs. Admittedly, they also gave the EU other mandates to regulate law enforcement and many other areas, such as public health, but those other mandates are much more limited, and their limits must be respected.

The conventional logic dictates expecting the legislators to be diligent *ex-ante* and the Court to punish them for laxity *ex post facto*. However, what should one do if, as shown above, legislators consciously bend the rules and the Court is pliable and plays along?

The only remaining option seems to be to re-negotiate the mandate, i.e., amend the relevant provisions of the TFEU. Particularly, the amendments could include a requirement for an evidence-based regulation and an expansion of the areas off-limits to market-making legal harmonisation contained in Article 114(2). This would contribute to blocking one of the avenues of the 'competence creep' and forming a definite agenda for EU harmonisation efforts that both the current and future Member States could identify in advance and rely on.

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CHAPTER 12

The Legal Basis for European Contract Law and the Tools to Achieve the EU's Internal Market

Ivan Sammut

Abstract

European legal integration can occur within the EU Treaty framework, with the legislation forming part of the European legal order or outside the Treaty framework, and it can be binding only under Public International Law. The significance of forming part of EU law is that it would only be binding in the EU Member States and that the Court of Justice of the European Union (CJEU) would play a role in ensuring the uniformity of interpretation through preliminary rulings. The law would have to pursue a Union objective stated in the Treaty. The author argues that harmonisation and/or unification of substantive private law is difficult to achieve outside the Treaty framework. If EU law and EU Contract law are to achieve their desired effect on the Internal Market, then the legal basis is of paramount importance.

1 Introduction

European legal integration can occur within the EU Treaty framework, with the legislation forming part of the European legal order or outside the Treaty framework, and it can be binding only under public international law. The significance of forming part of EU law is that it would only be binding in EU Member States and that the Court of Justice of the European Union (CJEU) would play a role in ensuring the uniformity of interpretation through preliminary rulings and the law would have to be in pursuance of a Union objective stated in the Treaty.[1] The harmonisation and/or unification of substantive private law is difficult to achieve outside the Treaty framework. However, if EU law and EU contract law are to achieve their desired effect on the Internal Market, then the legal basis is of paramount importance.

1 Craig, P., & DeBurca, G., *EU Law, Text Cases, and Materials*, (2nd ed.), OUP, Oxford, 1998, 110–123.

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2 The Legal Basis

As Professor Chalmers clearly explains in his textbook on EU law, each piece of EU legislation must be grounded on a legal base set out in the Treaty.[2] He explains that the legal basis has two main roles as follows:

> First, it enables the Community to legislate in the given field and sets out the scope for Community legislation in the area. Secondly, the legal base determines the legislative procedures and the type of laws that can be adopted.[3]

Two possible articles to be analysed as the legal basis for a potential Europeanisation of contract law are Article 115 TFEU and Article 114 TFEU. The first confers upon the Union the powers to harmonise legal provisions by the adoption of directives for the approximation of such laws, regulations or administrative provisions by the Council acting unanimously on a proposal from the Commission after consulting with the European Parliament for the establishment and proper functioning of the common market. The latter concerns adopting measures by a cooperation procedure to approximate provisions laid down by law, regulation, or administrative action in the Member States, which aim to establish and properly function the Internal Market. Both are mutually exclusive.[4]

One can see that while the former Article refers to a common market, the latter refers to an Internal Market. The Internal Market, unlike the common market, not only relates to the four freedoms but also involves the further integration of other economic policies to achieve an economic union. The restrictions imposed on the fundamental freedoms by Article 36 TFEU and the mandatory requirements under Article 34 TFEU[5] are compatible with the notion of a common market but not necessarily with the conditions of an Internal Market. It could thus be appreciated that the harmonisation/unification of private law is more in line with the demands of an Internal Market rather than just a common market. Since the Internal Market is broader, one could argue that Article 114 TFEU is more likely to be the legal basis for the Europeanisation of private law, especially a potential European contract

2 Chalmers, D., et al., *European Union Law—Text & Materials*, Cambridge University Press, 2006, 140.

3 *Ibid.,* 140.

4 In fact ex Article 95EC starts, "*By way of derogation from Article 94 …*".

5 Examples of the mandatory requirements are consumer protection, environmental protection & measures to combat unfair competition.

code.[6] However, reference should be made to the *Tobacco* case in this regard.[7] Article 114 TFEU cannot be used broadly. There must be proven grounds that the measure is necessary to attain the Internal Market. The conviction of a particular institution in itself may not suffice.[8] Van Gerven argues that Article 114 TFEU could be a legal base only where a measure of harmonisation, or unification, has genuinely as its objective the elimination of impediments to the freedoms with present or future obstacles to trade if they emerge. This is not the case where comprehensive unification is envisaged.

Another possible legal basis could be Article 352 TFEU, which provides for the authorisation of the Council to adopt regulations by unanimity if action is necessary to obtain one of the objectives of the Union and the Treaty has not provided the necessary powers elsewhere. However, this legal basis prevents the replacement of national laws with the proposed code. Unlike regulations adopted under the legal basis, the code would be an additional set of contract rules.[9] This would make this Article an unlikely legal basis for a code.

The TFEU also provides that to establish an area of freedom, security and justice progressively, the Council shall adopt measures in the field of judicial cooperation in civil matters as provided in Article 81 TFEU.[10] This Article, amended by the Amsterdam Treaty, opens the door for further harmonisation. However, it is connected to judicial cooperation in civil matters and has cross-border implications. López Rodrígues, referring to one of Lando's works in Danish, explains that he believes that Article 81 TFEU could be interpreted as a legal basis for the elimination of those obstacles to the good functioning of civil proceedings, if necessary, by promoting the compatibility of procedural rules.[11] One could argue that Article 81 TFEU is more likely to act as a legal basis for further unifying the conflict of contract laws.

Ex-Article 293 EC was another legal basis that could be examined. It permitted Member States, where necessary, to enter negotiations with each other to make conventions to secure benefits for their nationals, as was the case with the 1980 Rome Convention. However, such an article could not be the legal basis for a contract code since the powers that it confirmed were not sufficient

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6 Lopez Rodriguez, A. M., *Lex Mercatoria and Harmonisation of Contract Law in the EU*, Djøf Publishing, Copenhagen, 2003, 256.

7 Case C-376/98, [2000] *E.C.R.* I-8419, *Germany v Parliament and Council.*

8 See Van Gerven, W., "Codifying European Private Law? Yes, if …!", *E.L.Rev.*, 2002, 27: 165.

9 Basedow, J., "A Common Contract Law for the Common Market", *CMLRev.*, 1996, 33: 1169–1196 at 1187.

10 See ex – Article 61(c)EC.

11 Lopez Rodriguez, A. M. *op. cit.,* 258.

for such a purpose. This Article, however, served as the legal basis for the further harmonisation of private international law rules as stated above.[12]

The entry into force of the Amsterdam Treaty on 1 May 1999 brought new perspectives to harmonising contract law, particularly in conflict of laws. The insertion of the new Title IV, among other things, in the EC Treaty explicitly confers powers upon the Community to act within this field. The Amsterdam Treaty communautarised a substantial part of the third pillar of the TEU as established under the Maastricht Treaty.[13] The new conflict of laws powers given to the Community stems from ex-Article 65 EC as amended—the now Article 81 TFEU. Certainly, this was a step in the right direction from the perspective of European contract law and led to the conversion of the Rome Convention into a regulation.[14] However, certain difficulties could remain. For example, the Article provides for harmonisation necessary for the Internal Market's proper functioning. The link with the Internal Market may not be as clear as expected. It can be argued that the link with this aim is less apparent in a choice of law instrument, such as the Rome Convention, as it applies to cases where all objective factors, such as the parties' residence or the place of performance, are outside the Union. This difficulty might impede enacting the Convention as a regulation while retaining its universal scope.[15]

The impact of the Amsterdam Treaty has certainly been such that it has set the machinery in motion for further studies and proposals within this field. An example is the Action Plan the Council and the Commission drew up.[16] However, due to the Amsterdam communautarisation, Articles 81 and 114 of the TFEU found themselves at opposite ends of the community spectrum.[17] It could be argued that Article 81 TFEU refers to the aspect of the Internal Market of the free movement of persons. Other measures could be subject to Article 114 TFEU.[18] This is Israël's point of view. He bases his opinion on the proper construction of Article 81 TFEU and concludes that Article 114 TFEU is a better

12 Fauvarque-Cosson, B., "Comparative Law and Conflict of Laws: Allies or Enemies? New Perspectives on an Old Couple", 2001, *Am.J.Comp.L.* 49: 416.

13 Plender, R., *The European Contracts Convention—The Rome Convention on the Choice of Law for Contracts,* Sweet & Maxwell, London, 2001, 243.

14 Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I).

15 Plender R., *Ibid.,* 246.

16 Action Plan of December 3, 1998 of the Council and the Commission on how best to implement the provisions of the Treaty of Amsterdam on an area of freedom, security and justice, [1999] OJ C19/1–15.

17 Israël, J., "Conflict of Law and the EC after Amsterdam A Change for the Worse? (2000) *MJ.*, 7: 96.

18 Israël, J., *supra* 97.

legal base.[19] With this argument in mind, one would have to prove that the harmonisation of contract law is necessary for the free movement of persons. While on the other hand, one could disagree that Article 81 TFEU does not refer to the free movement of persons. Whatever view one holds, one could still conclude that Article 81 TFEU could act as a legal basis for harmonising the conflict of rules. It is certain that the clearer the rules relating to contract law, the more they could facilitate, albeit in an indirect way, the free movement of persons.

As regards the impact that the Treaty of Amsterdam would leave on the Europeanisation of private law, Bentem and Hondius argue that neither the First nor the Third Pillar is a good grounding for a complete codification of European private law. They concluded that:[20]

> For specific legal fields such as private international law and the law of civil procedure, possibly supplemented by some items of substantive law, the Treaty of Amsterdam is an excellent operating base. For the remainder of private law, attention should, for the time being, continue to be given to private legislative initiatives such as that of the Lando Commission.

According to the principle of subsidiarity[21] in areas which do not fall within its exclusive competence, the Union shall take action only if and insofar as the objective of the proposed action cannot be sufficiently achieved by the Member States and can, therefore, because of the scale or effects of the proposed action, be achieved by the Union. As regards the Europeanisation of contract law, it has to be determined whether such a process falls under the exclusive competence of the Union. Since such harmonisation/unification would be regarded as a measure proposed for establishing the Internal Market, the question may be as follows: Does the Union have exclusive competence to complete the Internal Market? If the answer is affirmative, the principle of subsidiarity would be out of the question. A possible interpretation also advocated by the European Commission is that the Union has exclusive competence for all actions that purport to establish the Internal Market. The Council has also adopted an interpretation reflected in texts such as the Time-Sharing Directive.[22] Another interpretation favours a concurrent competence of the Union and the Member States.[23]

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19 Israël, J., *supra* 97.

20 Betlam, G., & Hondius, E., "European Private Law after the Amsterdam Treaty", 2001, *ERPL*, 9: 20.

21 Ex Article 5EC.

22 See Remien, O., "European Private International Law, The European Community and its Emerging Area of Freedom, Security and Justice", *CMLRev.*, 2001, 38: 53–87.

23 See Basedow, J., "A Common Contract Law for the Common Market", *CMLRev.*, 1996, 33: 1169–1196 at 1191.

A second issue to be raised about the principle of subsidiarity is that even if there is concurrent competence of the Member States and the Union to harmonise certain fields of private law, notably contract law, can such an enterprise be sufficiently achieved by the Member States or can it, because of the scale and effects of the proposed action, be achieved by the Union? This question must be answered in the affirmative, as a single Member State cannot attain European uniformity by its laws.[24] Under this premise, adopting harmonised/unified private law, such as a contract code at the EU level, would be consistent with the principle of subsidiarity. However, it is arguable whether the EU could base such an enterprise on a provision of the TFEU. Nevertheless, on the said legal basis, several legislative initiatives have already been taken in private law, both in the substantive and conflict of laws fields. An analysis of these could provide practical examples of how the Europeanisation of contract law can be achieved.

3 The Tools to achieve European Contract Law

The most important tools that can be analysed are cooperation, harmonisation, uniformisation, unification and codification. As some writers may use different connotations for each term, it is important to clarify the meaning attributed in this work to each terminology at this stage. In the table below, one can find a list of tools that will be analysed, starting with cooperation, which is the least integrationist, and going chronologically towards the most integrationist tool, i.e., unification (Table 12.1). This table is followed by another table later in this paper, which includes the definition and characteristics of Codification (Table 12.2 of this paper). Codification/consolidation does not fit into the chronology of Table 12.1 as per the definition, given that it can be applied to the results of most of the tools listed in the table.[25]

3.1 *Cooperation*

Cooperation involves consultation between Member States to coordinate the converging of their national law. The TFEU provides for the "coordination", "approximation", and "harmonisation" of national legislation in various domains. Although the latter two have the same meaning in EU legal jargon, "harmonisation" is often preferred. Coordination came to be regarded as

24 *Ibid*., 1192–1193.

25 Sammut, I., "Tying the Knot in European Private Law", 2009, *European Review of Private Law*, 17: 813–840.

TABLE 12.1 The tools and their characteristics

Tool	Definition	Level of integration	Main characteristics
1. Cooperation	Consultation between Member States on legislative initiatives	Minimal	– Very partial – Very unsystematic – Dynamic
2. Approximation or Harmonisation	Legal rules from different jurisdictions are brought closer to each other in scope	Minimal to Comprehensive with varying degrees of integration	– Partial – Unsystematic – Two levels of governance – Dynamic
3. Uniformisation or Standardisation	Legal rules from different jurisdictions are similar to each other in scope	Comprehensive to almost Complete	– Partial leaning towards Comprehensive – Unsystematic – Two levels of governance – Less Dynamic
4. Unification	A supranational legal rule applicable in all Member States	Complete	– Complete – Could be systematic – One level of governance – Static

denoting a different and more superficial action than the other two terms.[26] Thus, one can say that cooperation is a very loose form of harmonisation. Cooperation (unlike harmonisation by a legal instrument) may occur through soft forms of integration, such as informal agreements between Member States or through soft-law initiatives. It is the least integrationist of all the tools and does not include formal steps to achieve the Europeanisation of private law. It could be used for those areas that are under the reserved competence of the Member States. Cooperation is, therefore, a very weak tool for Europeanisation if the Community Method is employed. However, it can be a very important

26 Dembour, M., "Harmonisation and the Construction of Europe: Variations away from a Musical Theme", *EUI* Law No. 96/4, 1996, 5.

tool when innovative modes of governance are resorted to, as cooperation may go beyond the remits allowed by the Community Method.

3.2 *Approximation or Harmonisation*

Harmonisation or, approximation, or coordination[27] is the process whereby legal rules from different jurisdictions are brought closer to each other in scope.[28] Harmonisation is a common method used by the European Union to bring the laws of the Member States closer to each other through directives to achieve the Internal Market. An important characteristic of directives affecting the new European legal culture is that a directive leads to "Impressionistic harmonisation".[29] In most legal systems, directives deal with specific subjects that form part of a broader subject, which may be systematically connected with other subjects. This patchwork, characteristic of the harmonisation of directives, is a direct result of the instrumental approach to law.

The Commission from which directives originate is concerned with specific changes in the law that it may regard as necessary to fulfil the function of the Internal Market and which are politically desirable. The directive is not concerned with the result it may have on the national legal system, and the same effect could vary from one system to another. This functional and impressionistic approach to private law could lead to friction within the national legal systems. While the directives aim at unity at the European level, they may cause disunity at the national level.[30] The disruptive effect is a direct result of the impressionistic approach. As Muller-Graff argues, to make matters even worse, directives are frequently incoherent among themselves.[31] This has led to the impressionistic approach being lamented by private scholars and is one of the main reasons for pleas for a systematic unification in the form of a European Civil Code.[32] Given the above nature of the tool, harmonisation is a very popular and important tool to be utilised with the traditional mode of governance.

3.3 *Uniformisation or Standardisation*

Uniformisation or Standardisation is perfect harmonisation. It involves achieving a perfect harmonised law, thus making the law of one legal order

27 These are different terms that are sometimes used interchangeably in the EC Treaty, for example, Article 6, 27, 40 41, 43, 54(3) (g), 56, 57, 63, 70, 75, 99, 100, 101, 102, 105, 111, 112, 113, 145, 220 and 235 (numbering as stood before the Amsterdam amendments).

28 Zapiriou, G., "Harmonisation of Private Rules between Civil and Common Law Jurisdictions", *The American Journal of Comparative Law*, 1990, Vol. 38, 71.

29 Hesselink, M. W., *The New European Private Law*, Kluwer, 2002, 36.

30 Joerges, C., *op. cit.*, 385.

31 Muller-Graff, P. C., "EC Directives as a Means of Private Law Unification", *op. cit.*, 77.

32 Lando, O., & Beale, H. (eds.), *Principles of European Contract Law*, Parts I and II, Prepared by the Commission on European Contract Law, The Hague, 2000, XXII.

identical to that of the others. With uniformisation, the laws of the Member States would be identical, but the rules of law would remain at the national level. Perfect harmonisation brings uniformisation. While some authors, such as George Zaphiriou, would prefer to use the same meaning for uniformisation and unification, a different meaning will be used for unification in this work.[33] Uniformisation may appear to be similar to the next tool: Unification. However, it is not similar, as explained in the next section. The tool is also very important if one adopts an innovative mode of governance for EPL.

3.4 *Unification*

Unification can be understood to refer to the instance when a supreme law legislated at a supranational level is set to apply in all Member States. Thus, with unification, the talk is no longer about national legal orders but is at the European legal order level. Unification would mean perfect Europeanisation. Unification is also used by the said Union when there is a need for a law operating at the Union level to regulate a particular aspect. The legal instrument used is a regulation. This makes this tool the one which achieves the most comprehensive Europeanisation under the traditional mode of governance. However, it has no use for innovative modes of Governance.

Nevertheless, some of the results which can be achieved by this tool, such as having the same private laws in substance in the Member States, can also be reached by the previous tool if the innovative mode of governance is used. With unification, one would have the same regulation in force across the EU. With uniformisation/standardisation, one would have the laws of the Member States identical or similar to one another.

4 Some Common Characteristics of the Tools

Unification and harmonisation can be achieved through similar means such as custom, trade practice, legislative acts and judicial practice, and academic writing.[34] Such processes can occur within a nation, between states or provinces of a federation or within a community of states, as in the case of the European Union. In Europe, unification and harmonisation were achieved in the past by the creation or reception of civil and commercial codes. In the US, several areas of law, such as copyright, antitrust and taxation, were unified

33 *Ibid*., 71.

34 See Bodenhiemer, E., "Doctrine as a Source of the International Unification of Law", *AmJ.CompL* 34: 67 (Supplement 1986), p. 67 ff also at www.cisg.law.pace.edu/cisg/biblio/bodenheimer.html.

by federal law at both statutory and judicial levels. The adoption of the Uniform Commercial Code achieved a different kind of unification.[35] Unification or harmonisation can be systematic, occurring within a particular legal tradition or between two different legal traditions. At their inception, the Civil law and Common law traditions were homogeneous. However, these were adopted by different countries and, therefore, subjected to the antithetical process of diversification and harmonisation.

Harmonisation and unification are merely methods to bring different legal orders closer to each other. The success and type of method used often depend on the aims behind such projects. Whether the Union uses one method or the other depends on the competence of the Union in the particular subject area and on whether the principle of subsidiarity is satisfied. Private law is a generic term that includes a wide area of substantive rules of a legal system. What might be relevant for contract law may not necessarily be for family law.[36] Thus, after examining in detail the results that the said methods can achieve, it makes sense to briefly examine in the following chapter how the said tools could be used for some of the most important areas of substantive private law.

When dealing with harmonisation and unification, one has to consider the issue of legal irritants. European directives may often contain legal concepts alien to the national legal systems. These legal irritants occur when a legal transplant, as described in the next chapter, is, to a certain degree, not very successful.[37] A particular example is the attempt to introduce the notion of good faith into English law due to the transposition of the Unfair Terms Directive.[38] The problem that arose related to the scoping of whether it should become part of the general clause as it stood in the civil law system or whether its field of application should be limited to the content of standard terms in consumer contracts. The legal irritants may have yet another disruptive effect on the coherence of the national system. Since the EU has had directives since its inception as the EEC more than half a century ago, directives are now a way of life in the European legal system. This means the European legal systems had to adapt to a new reality. So, when analysing the impact of harmonisation and unification, one should assess the impact of these tools to prove whether more Europeanisation is achievable.[39]

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35 See Zapiriou, G., *op. cit*., 72–73.

36 Barnett, G., & Berardeau, L., *Towards a European Civil Code,* ERA, Trier, 2002, 10 ff.

37 Teubner, G., "Legal Irritants: Good Faith in British Law or How Unifying Law Ends Up in New Divergences", *MLR* 1998, 1 ff.

38 Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts.

39 Sammut, I., "Tying the Knot in European Private Law", 2009, *European Review of Private Law,* 17: 813–840.

5 Codification/Consolidation

Codification is collecting and restating a jurisdiction's law in certain areas, usually by subject, possibly forming a legal code. By "law" here, one means any legal instrument. Thus, collecting any legal instrument into one instrument is a codification process. Thus, it is wrong to associate unification with codification as it could be applied to any of the previously mentioned tools. For example, Directive 2004/38/EC could also be described as a codification process of the previous harmonisation directives.[40] Here, one can perhaps make a slight distinction between codification and consolidation. The latter involves freezing existing legislation into a consolidated version, while the former may see the introduction of new elements in the consolidation process. Codification can also be understood to be the process of enacting laws such as civil codes. This is maximum codification. In this chapter, the term codification is not restricted to maximum codification but is used to describe the process mentioned in the first part of this paragraph. Therefore, codification falls outside the hierarchical order described in Table 12.1. Table 12.2 provides the characteristics of codification.

TABLE 12.2 Codification/Consolidation

	Definition	**Level of integration**	**Characteristics**
Codification/ Consolidation	A process of collecting and restating the law of a jurisdiction in certain areas, usually by subject, possibly forming a legal code	Comprehensive, particularly in a selected area	– Comprehensive – Systematic – Often, one level of governance – Static but can be changed

40 European Parliament and Council Directive **2004/38/EC** of 29 April 2004 on the rights of citizens of the Union and their family members to move and reside freely within the territory of the Member States amending Regulation (EEC) No **1612/68** and repealing Directives **64/221/EEC**, **68/360/EEC**, **72/194/EEC**, **73/148/EEC**, **75/34/EEC**, **75/35/EEC**, **90/364/EEC**, **90/365/EEC** & **93/96/EEC**, OJ L 158 of 30.04.2004.

6 Conclusion

In the present-day EU, the basic nineteenth-century situation in which each nation-state had its legal system still prevails. The codes have survived on the continent, and the nation-states are still strong. There does not appear to be any credible sign that the peoples of Europe wish otherwise. R. C. van Caenegem speaks of "one nation, one state, one code of law".[41] The same holds in the Anglo-Saxon world, where the uncodified English law's hold on England and Wales is still very powerful as they prefer to adapt and evolve to modern needs in their ways. While the tools contribute towards the approximation or unification of law as the legal traditions are not in limbo, an issue that remains to be discussed is what form the harmonised or unified law should take. Should it be built upon a codified system, or should it be built around the common law format? The answer to this question depends on which tool is used. Harmonisation, even if comprehensive, does not lead to a unified law system, so the nation-state law is preserved as it is, at least in its current form. The legal basis sets the limits on what can be achieved. Unless the Member States wish more integration and increase the reach of the legal basis, European Contract law will likely evolve through more fragmentation as long as there can be a justification in the interests of the Internal Market.

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CHAPTER 13

Internal Taxation in the EU's Internal Market: Is Article 110 TFEU All about Protectionism?

Ivan Sammut

Abstract

This paper looks at the evolution of Article 110 TFEU through the Court of Justice of the European Union's main cases. Such a phenomenon often occurs through the imposition of discriminatory taxation upon goods originating in another Member State with the intent and effect of promoting the locally produced good. Situations are reminiscent of the latter circumstances and can thus impede one of the four freedoms central to the proper functioning of the European Union, proving a hindrance to the free circulation of goods between the Member States. Thus, mechanisms preventing the application of such discriminatory measures through internal taxation are imperative. At face value, the wording of the article prevents discriminatory indirect taxation upon goods that are either similar or capable of competing. This said internal taxation may nonetheless be differential yet not discriminatory. The latter applies when there is an objectively justifiable reason for imposing a higher tax on goods originating in another Member State than that imposed upon the domestic product. Finally, the paper compares and contrasts jurisprudence to examine if an element of protectionism is needed for a national measure to be caught up by Article 110 TFEU.

1 Introduction – the Objectives of Article 110 TFEU

Over the past decades, one can appreciate that the underlying rationale of the Internal Market is to produce an economic union where goods move freely within the Union's borders. This involves eliminating all differences between individual economists capable of impairing the flow of factors, that is, preferences based on nationality, after becoming relevant. However, the objective of Article 110 TFEU is to prohibit discrimination based on nationality. It does not seem to aim at making taxation provisions identical, merely to cleanse them of discrimination. The consistent case law of the CJEU has noted that Member States can operate different systems of taxation to reflect different social and

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economic goals. However, such differential systems cannot infringe the principle of non-discrimination.

The Court appears to place little or no value on the similarity of national tax regimes. Not only is the goal of this harmonisation imperfectly recognised by the TFEU, but it is also a very contentious political issue. According to several case laws, the Court suggests that the primary function of Article 110 TFEU is to prevent discrimination and internal tax matters based on nationality. Regarding Article 110 TFEU (Ex Article 95 EEC pre 1999 and ex Article 90 EC pre 2009), the Court of Justice in the *Bobie* case said:[1]

> Article 95 seeks to ensure, by means of the prohibition which it lays down, that an importing Member State does not, by means of internal taxation of imported products and similar domestic products, give domestic traders preferential treatment as compared with their competitors from other Member States who sell similar products on the market of that State.

This statement has been followed in several other cases. Also, one may have to examine the difference between this provision's first and second paragraphs. The first reads that "no Member State shall impose, directly or indirectly, on the products of other Member States any internal taxation of any kind in excess of that imposed directly or indirectly on similar domestic products". The second paragraph reads that "furthermore, no Member State shall impose on the products of other Member States any internal taxation of such a nature as to afford protection to other products". The first difference between the two paragraphs is the use of 'similar' in the first paragraph and 'other products' in the second paragraph. The scope of Article 110 TFEU paragraph 1 differs from that of Article 110 paragraph 2 in that the former is more narrow. This brings the question: what does comparable mean? From the *Spirits* case decided in 1980,[2] the Court draws an indistinct line between 'similar products' under the first paragraph and 'other products' under the second.

2 The Context

Through protectionism, one can understand the difference between discrimination based on the product's nature and discrimination based on the product's nationality. Protectionism involves the latter and not the former.

1 Case 127/75.

2 See Case 168/78.

Article 110 TFEU does not stop Member States from taxing whisky more than wine or beer. That is within the discretion of the Member State. It, though, prevents Member States from offering an advantage to the local product over that of another Member State through taxation. A Member State may decide that whisky is a cause of alcoholism and beer is not, and vice versa. A Member State can decide to tax the protection of synthetic alcohol more than alcohol distilled from surplus food even though the products are chemically identical, and there is no obligation on the Member States to treat similar comparable products identically.

What a Member State cannot do is make choices based on the nationality of the product or the producer. If a Member State says all foreign cheese is to be taxed at 15% and the domestic equivalent at 5%, there is discrimination based on nationality. On the other hand, suppose a Member State requires all the wine with a designated appellation, whatever its origin, to be considered a luxury product and is taxed at 100%. In contrast, the undesignated wine is taxed at 5%, and the system does not appear discriminatory. However, if there is no system of appellation for wines produced in the importing Member State, then the clear rule is that there cannot be discrimination based on nationality. Member States can discriminate between products, but this discrimination cannot affect or be based on the product's nationality. Objective criteria must be used to differentiate products, and defining the product correctly is essential. The definition of a product has two competing aspects. If the product is narrowly defined, for example, only diesel cars instead of cars in general, it is relatively easy to claim discrimination. The product coverage of the discrimination is, by definition, narrow. This would mean the effect of the ruling striking down discriminatory legislation introduced.

On the other hand, an expansive definition of a product that is all cars rather than just diesel cars includes a wide product base, but discrimination across such a wide base is more difficult to prove. For example, the *Italian VAT diesel cars*[3] is a typical case where the Commission argued that the Court should consider discrimination only concerning diesel cars. The Court did not follow the suggestion, arguing that the relative products were cars in general, i.e. both petrol and diesel. At that time, electric cars were not on the market. The choice of product was crucial. Had the Court followed the Commission's suggestion, there would have been no Italian products suffering the highest tax rate. This would have raised the question of the protection of Italian products. As it happened, by choosing the category of cars, Italian petrol cars were taxed

3 See Case 200/85.

at a higher rate. Therefore, Italian products indeed suffered as a result of the tax criteria. One can conclude that the Court seems to have chosen the products with a view to the case's outcome. This might support an argument that the Court was looking to the intent underlying the Italian law and ignoring the effect of the law on the diesel car market.

So, does the Court first examine the intention behind the national legislation and then select the products? This is also another contentious argument to make. One could conclude that a possible way of explaining the Court's diverging behaviour concerning product organisation is that, in some cases, the Court seems to say that everything is comparable. In contrast, in other cases, it is also a very close and objective distinction which could have been previously disregarded. So, how could one conclude what the Court would decide when interpreting Article 110 TFEU?

First, the Court looks to the intent underlying the statute. If the law discriminates between domestic and foreign products, the Court will strike down the law since it intends to protect domestic production. On the other hand, if the statute is not formally discriminatory and pursues a policy that does not discriminate between products based on nationality, then it will be upheld. However, one has to consider the following considerations. Suppose the law is formally non-discriminatory but is intended to operate politically so that only domestic products qualify for prevention and treatment. In that case, the Court may strike it down since the notion presumed is to intend to protect domestic production. Secondly, suppose the law is formally non-discriminatory but operates so that a significant amount of the foreign product is denied the full preferential tax treatment. In that case, the Court may also strike down the national legislation since there is evidence of the protection of domestic production. For example, if only the domestic product is in the low-tax band, and only the following products are in the high-tax band, the presumption of protection is the strongest. If a mixture of foreign and domestic production is in the lower band, and only the following goods are in the high end, then the presumption of protection is stronger but not as strong as in the previous case. If only domestic production is in the low-tax strength and the mixture of foreign and domestic is in the high-tax band, then the presumption of protectionism is weak. Finally, where even a mixture of both domestic and foreign goods appear in both categories, then there is probably no presumption of any protectionism.

Regarding the connection with the intended effect, the Court will strike down the tax if the law has a protectionist purpose. On the other hand, if the effect is protectionist but the purpose is not met, the Court may still uphold the law. What does one mean by protectionist or discriminatory law? The

Court's classification as protectionism when the national law protects local goods seems appropriate when it aims to protect domestic products against competing imported products. However, it is not necessarily connected with the exclusive purpose in mind. Should the protectionist purpose, which is not the only purpose of the specific exploration, be considered by the Court as sufficient to render the law protectionist? Concerning the objective of non-discrimination pursued by the Court and the cases decided so far, protectionism does not have to be the law's main purpose. The Court strikes down the law as long as it is apparent that it has the purpose of protectionism, which is one of the motives for its enactment. This permits the Court to scrutinise and strike down a large number of revenue losses and to pursue non-discrimination in a very powerful way.

3 The Nationality Hypothesis through the CJEU's cases

A good way of examining the hypothesis that the Court of Justice strikes down any internal tax law that can be deemed protectionist is by comparing several similar cases and seeing each case's outcome.

3.1 *Danish Fruit*[4] *v John Walker*[5]

In Denmark, the production of grapes and grape wine is practically impossible. There is, however, a substantial production of fruit wine, mostly from apples. Danish legislation taxed grape wine of the table type at a rate of DKR 10.725 per litre and grape wine of the liquor type at DKR 19.93 per litre. Fruit wine of the table type was taxed at DKR 6.92, and fruit wine of the liquor type at DKR 11.02 per litre. The total consumption of grape wine of both types was much greater than the total consumption of food wine of both types; however, the consumption of food wine of the liquor type was almost all produced in Denmark, while consumption of the grape wine of the liquor type has decreased in absolute numbers. The European Commission brought an action against Denmark, arguing that the tax was discriminatory. Grape and fruit wine should be considered similar by the legislator and taxed similarly, even if the two are not similar. The Commission argued that the two types of wine were at least in competition and that the tax system afforded indirect protection to domestic production.

4 Case 106/84.

5 Case 243/84.

Denmark denied the similarity of the competitive relationship between the two products. It also argued that the text did not have a protective effect. It represented the same percentage of the price even though there was a surcharge on wine if the base taken for composing was the volume of the alcoholic strength. Finally, Denmark argued that the purpose of the legislation was to guarantee food growers working in different climatic conditions sufficient income to support farmers growing local production. Under Danish law, imported fruit wine benefits from the favourable arrangement without considering production conditions. The Advocate General started by pointing out that the differential taxation of similar products could be justified when it pursued social and economic policy objectives compatible with the requirement of the Treaty; however, in the specific case, the purpose specified system, that is, the favourable treatment of certain agricultural products against certain other agricultural products was not compatible with the Treaty and the CAP. The tax system protected food producers in Denmark from imports from food producers. The Advocate General accepted in principle the Danish argument that if the tax is measured based on the price, the tax burden on the two products was the same; however, he then argued that notwithstanding similarity, fruit and grape wines of the table type were not similar.

The Court did not completely follow the AG's suggestion. In a rather short judgement, it was first noticed that the grape wine consumed in Denmark was completely imported while fruit wine of the liquor type was essentially domestic. Two-thirds of the fruit wine of the table type was domestically produced. It then pointed out that fruit wine of the table type has traditionally represented an essential market for domestic producers. It stated that to determine whether two products are similar, it is necessary to consider the objective characteristics of both categories of beverages, including their origin, method of manufacture, and other organoleptic properties. Then, they have to verify whether they meet the same consumer needs, keeping in mind that the test should not be assessed based on current consumer habits but rather take into account the prospective developments of these habits.

In the comparative case, a Danish court made a preliminary reference to the CJEU concerning the system of taxation and spirits in Denmark, particularly the Johnnie Walker case. In Denmark, spirits were taxed at a specific rate per litre of pure alcohol and an *ad valorem* duty. As one has already observed, the fruit wine of the liquor type was taxed according to different criteria, leading to an inferior global burden. Fruit wine of the liquor type is not considered spirit if the final alcoholic strength is less than 20%, even if ethyl alcohol was added to reach the desired strength. Walker, who exported whiskey to Denmark, argued that the taxation system was discriminatory. It favoured fruit liquors whose

production was domestic and spirits imported from other Member States. A bottle of fruit wine was only taxed at about 25% of the final price, while John Walker incurred a tax of 70%. There was no substantial difference between the two in terms of alcoholic strength. The production system was also similar because, in both cases, ethyl alcohol was added.

In line with the Advocate General's opinion, the Court denied that fruit wine and whiskey could be considered similar products. The Court pointed out that the physical characteristics and consumer needs should be given equal weight. The Court then stressed that the organoleptic qualities system of production, including fermentation and distillation, and consumers' habits regarding alcohol level led to the conclusion that the two products were fundamentally different. The Court turned to the second paragraph of Article 110 and pointed out that about 72% of the domestic production of alcoholic beverages was in the same tax bracket as whiskey; hence, there was no protectionism in this case, and the tax regime was upheld.

3.2 *Italian Sparkling Wines and Italian Marsala*[6] *vs French Sweet Wines*[7]

Marsala wine represented a large percentage of Italian wine production. According to the European Commission, it represented 90% of the total. The Italian system applied a manufacturing tax on domestic alcohol. In the *Marsala* case, the European Commission argued that the system protected the Marsala against similar competing liqueur wines imported from other Member States. Italy imposed this to help Marsala, an economically depressed region, improve economically. Italy argued that Marsala required a separate system of protection, which differentiated from any other one. In his opinion, the AG observed that the legislation was intended to encourage and protect the Marsala wine producers and that the criteria chosen by the legislator were non-objective. As a result, imported liquors were disadvantaged, with a substantial part of the domestic production taxed at a lower rate. The Court of Justice agreed with the opinion of the Advocate General. In the first place, it pointed out that only wines were similar products, which is the meaning of the first paragraph of Article 110 TFEU. It then turned to justifications brought by Italy. The Court argued that Italian law was designed in a way that would never consent to any foreign products to qualify for the designation of Marsala and, therefore, enjoy the reduced tax rate. The Italian text legislation was, therefore, clearly discriminatory.

6 Case 277/83.

7 Case 196/85.

Set against this background is a case dealing with the taxation of French national sweet wines. French legislation accorded favourable treatment to national sweet wines as against other sweets and liquor wines; initially, the treatment was accorded only to national sweet wines produced in France. After a formal opinion by the Commission, France extensively treated a national sweet wine produced in specific regions of the EU. The legislation stipulated conditions for foreign wine to meet before qualifying for treatment. After the Commission notified France, France complied again with some of the recommendations provided by the Commission's opinion; however, the Commission still proceeded to take action before the Court, arguing that further conditions in the legislation put foreign wine at a disadvantage. In particular, the Commission challenged that the product should come from a region where the production was traditional and customary.

The second challenge was requiring wines to be subjected to control guarantees equivalent to those required for national sweet wines. France justified the legislation by arguing that the production was carried out in regions with peculiar weather conditions where other agricultural products could not be produced, and the economy was largely dependent on that production. Both historical and technical significance justified the traditional requirement. Moreover, the legislation did not discriminate against other European products. For example, wine from other Member States' regions that could qualify for the objective criteria could also qualify under French law. Hence, the benefits were not exclusively to domestically produced French wine.

The Court of Justice upheld the French legislation. Regarding the traditional customer requirement, the Court argued that the policy pursued by France was consistent with EU law, and two points are particularly important. First is the analysis by the Court that accepted the suggestion coming from the Advocate General and did not discuss whether or not the French requirement was justified by compelling reasons as long as it was not formally or practically discriminatory. Then, the Court rejected the second objection and argued that a Member State was free to require the legislation of other Member States, which permits verifying the compliance of a particular imported product with the requirements set out by the national legislation. The requirement was, therefore, not unnecessarily restrictive.

Hence, one can compare the French and Italian cases here. In the *Marsala* case, Italian law was discriminatory without objective grounds from a national perspective. Italian law wanted to protect Italian products as opposed to imported products. On the other hand, the French case did not seek to protect the domestic product but rather the disadvantaged product. This meant that French and imported disadvantaged products could enjoy the protection of

French tax law. Hence, in the first case, there was an element of national protectionism; in the second French case, there was no national protectionism. Hence, similar cases concluded differently by the CJEU further prove that the CJEU, in interpreting Article 110 TFEU, looks at an element of protectionism as a major basis in determining whether Article 110 TFEU is infringed.

3.3 *Belgian Beer*[8] *and Wine v British Beer and Wine*[9]

These two cases are very similar to each other. Both deal with the drinking habits of beer instead of wine in their respective countries. The UK and Belgium have temperate climates and produce more beer than wine. Both countries also have populations that enjoy drinking. There was a higher tax on imported wine than locally produced beer in the UK and Belgium. In the UK, it was clear that consumers would purchase the cheapest alcoholic drink. If the tax is at a lower rate, this means that in the UK, consumers will end up purchasing more domestically produced beer as opposed to imported wine. In fact, during the five years of its membership, the UK had a transitory period within which it was allowed to offer favourable treatment. However, when the UK continued offering favourable treatment to locally produced beer instead of imported wine, the Court found that this breached Article 110 TFEU.

In Belgium, where wine is not produced, but there is substantial beer production, wine was still subjected to a higher rate than beer. The Commission brought an action against Belgium, arguing that the tax was discriminatory because, as determined by the Court in the UK case, there was a competitive relationship between Beer and wine. The Commission took the view that once a competitive relationship has been shown, any difference in the rate of tax applied to the same taxable base is contrary to Article 110 TFUE. Belgium argued that, on the contrary, under the second paragraph of Article 110 TFUE, it is necessary to ascertain whether the difference in tax burdens will likely affect consumers' choices. In this case, the difference in VAT rates was small and could not influence the consumer's choice. In all the other cases, verifying the competitive relationship and actual protective effect is necessary. The Advocate General then addressed the question based on the decision of the Court, and the British case took the view that the most intense competitive relationship existed between the most commonly consumed and substantially cheaper wine and beer, which represented the wider market sector.

In this area, the Advocate General compared tax burden and used it to assess the incidence of the price index. He concluded that no protective effect was

8 Case 356/85.

9 Case 170/78.

shown since the difference in price between wine and beer was such that the difference in tax rate was not enough to distort competition. He pointed out that this conclusion was confirmed by the fact that the consumption of wine in Belgium had increased while beer consumption decreased. In its examination of the tax system, the Court of Justice agreed with the conclusions of the Advocate General. Unlike the UK case, in the Belgium case, the difference in taxation between wine and beer was less marked, and the consumer behaviour in Belgium was much less price sensitive than in the UK. Consumers behaved differently in the different countries, so the effect of protectionism in Belgium was much less evident than in the UK.

In other words, the Belgian case was concluded differently from the British one, even though the facts were similar. The difference between the two seems to revolve around the tax system in the UK case. The UK did not deny that the system was originally designed to have a protective effect but tried to argue that there was no possibility of comparing the products. In the Belgian case, the VAT system was a general taxation system applicable to thousands of products. Coincidentally, it appeared to discriminate between foreign and domestic products somewhere over its application range. Certainly, such an effect was unintentional.

4 Conclusion

While the cases analysed above go back to the early years of the Internal Market, and they may be considered old cases, they are still highly relevant today. One would expect these judgments to remain important well into the next decade and beyond. These cases are only samples. One can also mention, for example, the Italian *diesel car* cases mentioned earlier in this paper and the *Humblot* judgment[10] regarding car registration taxes, among others. The Court of Justice has mainly taken a protectionist approach in the sense that the Member States retain full freedom to impose any indirect tax they deem fit as long as the implementation of this tax is not done in such a way as to afford protection to domestically produced goods over goods imported from other Member States. Hence, one can conclude that Article 110 TFEU does present a strong element of protectionism in its implementation and ensures that Member States do not discriminate based on nationality when implementing rules and taxation. Unlike customs duties between Member States, which are

10 Case 112/84.

completely prohibited with no exceptions, internal taxation is allowed as long as it is not discriminatory. Thus, one can conclude that protectionism plays a very important role in the implementation, interpretation and application of Article 110 TFEU.

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CHAPTER 14

Not Guilty: Do Non-Conviction-Based Confiscations Go Too Far?

Ilona Schembri

Abstract

Criminal activity hinders EU Internal Market growth by reducing trust between citizens, and illicit profits infiltrate the legal economy. This phenomenon has led the EU to enact a directive regulating illegal asset freezing and confiscation. In addition, it has issued a regulation that facilitates cross-border freezing and confiscation orders. However, traditional freezing and confiscation measures do not provide sufficient results, leading to the implementation of more effective measures. Non-conviction-based confiscation is the most viable alternative, in which assets of not criminally convicted people are confiscated if they cannot prove legitimacy. Taking such measures to combat criminality may violate a person's human rights. Therefore, this paper will explore the dynamics of non-conviction-based confiscation and human rights violations.

1 Introduction

Legislators only began considering non-conviction-based confiscations this past twenty-five years when it became clear that the traditional approach to combating criminality was insufficient to deter crime.[1] Criminals have learned over the years that they must use more sophisticated laundering schemes, making it difficult for law enforcers to establish a direct link between criminal offences and proceeds.

This paper defines non-conviction-based confiscation and examines whether legislators took it too far in their fight against criminality. This analysis will also examine how these modes of confiscation protect citizens' rights as a society and as individuals. Using desk-based research and the various documents published by the EU and international organisations, this paper will determine whether States must implement a model of non-conviction-based

1 Council of Europe, 'The Use of Non-Conviction Based Seizure and Confiscation', <1680a0b9d3 (coe.int)> accessed 27 March 2024.

 | DOI:10.1163/9789004712119_016

confiscation to combat criminality while protecting the rights of their citizens effectively.

2 Definition of Non-Conviction-Based Confiscation

One requisite differentiates criminal confiscation from non-conviction-based confiscation. A conviction is not required in the latter case but is required for criminal confiscation. Lawmakers take this approach since they consider non-conviction-based confiscation a civil matter, while conviction-based confiscations are criminal matters, and criminal law principles apply.

It appears, however, that in three out of four non-conviction-based confiscation models that will be discussed in the following section, there is a relationship between non-conviction-based confiscations and conviction-based confiscations because there must be a link between the proceeds of crime and the criminal offence in a non-conviction-based confiscation as much as in a conviction-based confiscation.

3 The Four Models of a Non-Conviction-Based Confiscation

No law or case law categorises the different forms of non-conviction-based confiscation despite legislators agreeing that there is no conviction in a non-conviction-based confiscation. Such work was only conducted nine years ago by an organization. The Camden Asset Recovery Inter-Agency Network (CARIN)[2], funded by the European Union (EU), developed the four models concerning the non-conviction-based confiscation typologies in 2015, and are reproduced below.

Model 1: This classic non-conviction-based confiscation applies if confiscation cannot be based on a final conviction. While proceedings have been instituted against an accused, they cannot be concluded. In this scenario, the offender cannot be brought before the court or convicted because the accused has died, absconded, or is deemed unfit for prosecution because of immunity, age, or mental state.

Model 2: The extended confiscation procedure allows confiscating assets unrelated to the crime for which the offender is prosecuted and found guilty. Therefore, the order to confiscate extends to assets owned by the defendant that are not directly related to the criminal offence.

2 CARIN is an informal network of law enforcement agencies sharing knowledge and information on tracing assets in a member's country.

Model 3: Assets obtained illegally are confiscated through *in rem* proceedings (actions against the property, not the individual). Therefore, action is taken also against third parties holding the property for the defendant.

Model 4: The unexplained wealth model compares a person's assets with their income. An indirect or direct link to a predicate offence is not required.

4 The Protection of Citizens' Human Rights

A fundamental principle of criminal law is that anyone can be a victim. Victim studies have been at the forefront only for the past fifty years,[3] with a greater emphasis in the 21st century.[4] Also, the term 'victim' was only specifically defined in the past twelve years. In 2012, the European Union enacted Directive 2012/29/EU that defined such a term. The Maltese law, for example, transposed this Directive in 2015, and it defined victims per the Directive, which stipulates, among other things, a "natural person who has suffered harm, including physical, mental or emotional harm or economic loss which was directly caused by a criminal offence including harm from terrorist activities".[5] This definition reinforces the principle that the State must protect citizens' rights, as victims, by combating criminality, even more so when such a definition demonstrates that criminality threatens a country's stability. As a result, confiscations without conviction became more popular.

However, legislators must ensure that while defending society's rights, individuals' rights cannot be undermined and must be preserved. The European Court of Human Rights (ECtHR) has had the opportunity in various judgments to examine whether non-conviction-based confiscations violates individual rights, specifically violations of Article 1 of Protocol 1 and Article 6 of the European Convention on Human Rights (ECHR).

5 Applicability with Article 1 of Protocol 1

This Article regulates property right and specifies three rules guaranteeing this right. First, it lays down the principle of peaceful enjoyment of property in the

3 Joanna Shapland, 'Victims, the Criminal Justice System and Compensation', *The British Journal of Criminology* 24, no. 2 (1984): 131–49. <http://www.jstor.org/stable/23637025> accessed 27 March 2024.

4 Viacheslav Tuliakov, 'Criminal Law and its Victim-Oriented Development: An Academic Inquiry', part of the book Copernicus, Political and Legal Studies, Vol. 2, Issue 3 (September 2023): pp. 70–74.

5 Victims of Crime Act, Chapter 539 of the Laws of Malta.

first sentence of the first paragraph. The second rule in the same paragraph then covers the deprivation of possessions, which can only occur according to law and the general principles of international law. The third rule emanates from the second paragraph, which states that the Contracting States are allowed to control property use in accordance with society's general interest[6], which interest seems to be beyond the legal provisions "to secure the payment of taxes or other contributions or penalties".[7] This third rule establishes that the principles governing the question of justification of a confiscation order are that the interference must be lawful and in the public interest where such interference must, therefore, strike a balance between the general interests and the rights of respondents, and thus, against those persons whom a petition is filed.[8] While the second exception, or rule, is easy to determine as one only needs to examine the wording of the law, the third exception, or rule that emanates from the second paragraph is difficult to determine as it is imperative to understand what lawfulness means and how States can achieve the general interest by balancing citizens' and individuals' human rights with lawfulness and general interest.

5.1 *Lawfulness of the State Interference*

From a first glance, 'lawfulness' means that the State has a right to interfere because the law allows the State to do so. Hannah Arendt describes such a term as "the only legitimate content of human living together and all political activity is ultimately devised as legislation or application of legal prescriptions".[9]

However, the ECtHR had the opportunity to define such a term in various judgments whereby it held that "the requirement of lawfulness, within the meaning of the Convention, demands compliance with the relevant provisions of domestic law and compatibility with the rule of law, which includes freedom from arbitrariness".[10] Accordingly, lawfulness does not only refer to legislation but also to legitimacy, and therefore, "that is, in conformity with the

6 European Court of Human Rights, 'Guide on Article 1 of Protocol No. 1 to the European Convention on Human Rights, Protection of property', 31 August 2022, <Guide_Art_1 _Protocol_1_ENG (coe.int)> accessed 28 March 2024.

7 Equality and Human Rights Commission, 'Article 1 of the First Protocol: Protection of property', 3 June 2021, <Article 1 of the First Protocol: Protection of property | EHRC (equalityhumanrights.com)> accessed 26 March 2024.

8 *Denisova and Moiseyeva v. Russia*, no. 16903/03, para. 55, 1 April 2010, Ünsped Paket Servisi SaN. Ve TiC. *A.Ş. v. Bulgaria*, no. 3503/08, paras. 39–40, 13 October 2015.

9 Hannah Arendt, 'The Great Tradition: I. Law and Power', *Social Research* 74, no. 3 (2007): 713–26. <http://www.jstor.org/stable/40972121> accessed 28 March 2024.

10 *East West Alliance Limited v. Ukraine*, no. 19336/04, para. 167, 2 June 2014, , Ünsped *Paket Servisi SaN. Ve TiC. A.Ş. v. Bulgaria*, no. 3503/08, paras. 39–40, 13 October 2015.

values and beliefs of the society".[11] The ECHR does not define the rule of law or arbitrariness, but defining these terms is crucial to understanding the scope of property rights.

5.2 *Rule of Law and Arbitrariness*

The rule of law and arbitrariness are interlinked because the ECtHR goes even further than considering violations against the law by referring to the term arbitrariness. In this respect, the United Nations Human Rights Commissioner has defined arbitrariness as "not to be equated with 'against the law', but must be interpreted more broadly to include elements of inappropriateness, injustice, lack of predictability and due process of law".[12]

The Venice Commission, one of the Council of Europe's advisory bodies composed of independent constitutional lawyers, outlines the definition of the rule of law in detail and divides it into five sub-headings:[13]

1. Legality

   Democracies are founded on the principle of legality. The supremacy of the law requires that State actions be according to the law and authorised by the said law. Accordingly, the law must define the relationship between international and national law. However, it must also outline the circumstances in which exceptional measures can derogate from the human rights regime, which can be for legitimate reasons.

2. Legal Certainty

   This legality must be based on legal certainty. Legal certainty varies depending on the area of law because laws are interpreted and applied differently. In criminal law, for example, legal certainty is anchored by basic principles such as *nullum crime sine lege/nulla poena sine lege* and non-retroactivity.

   Legal certainty is based on three principles: first, the law must be clear; second, it must be foreseeable; and third, the law must be easy to understand. While the first and the third requirements are undisputed, the foreseeable principle can be disputed because it can be subjectively defined. In various ECHR opinions, the foreseeability requirement is still

11 R. W. Smith, 'The Concept of Legitimacy', Theoria: *A Journal of Social and Political Theory*, October 1970, No. 35 (October 1970), pp. 17–2, <https://www.jstor.org/stable/41801858> accessed 28 March 2024.

12 About arbitrary detention | OHCHR> accessed 27 March 2024.

13 Council of Europe, Venice Commission, 'Rule of Law', <Venice Commission: Council of Europe (coe.int)> (accessed 27 March 2024>

met even if the individual concerned must seek appropriate legal advice to determine the consequences of a specific action.[14]

The ECtHR discussed the legal certainty concept in ***Markus v. Latvia***,[15] whereby the Court ruled that a confiscation punishment was unlawful since the impugned domestic regulation lacked clarity, foreseeability, and procedural safeguards and afforded no protection against arbitrariness. In this case, the property was confiscated as an ancillary penalty. However, the domestic Court did not specify the property to be confiscated; instead, the measure was applied to all properties owned by the respondent. The ECtHR has held that where regulation leaves uncertainties regarding the trial court's competence, it is not foreseeable and does not protect against arbitrariness. Additionally, it may seriously impair someone's ability to present their case in Court effectively.

3. Prevention of Abuse of Powers

To prevent abuses of power, the legal system must provide safeguards against arbitrariness so that the discretionary power of officials is limited and regulated. In the Venice Commission, misuse of power is also discussed, but abuse of power is synonymous with misuse when such misuse develops into a habit. Thus, the difference between misuse and abuse of power is that misuse results from negligence, ignorance, or an emergency, while abuse arises from habitually misusing something.

Public hearings are an essential part of the principle of a fair hearing that fights arbitrariness resulting in less power abuse. In ***Kilin v. Russia***,[16] the ECtHR reiterated that the (non-)violation of the defendant's right to a public hearing does not necessarily signal actual damages. Although an applicant would otherwise have an adequate opportunity to present his defence concerning his right to an oral hearing, equal arms, and adversarial procedure, the authorities must demonstrate that the decision to hold a non-public hearing is strictly necessary for the circumstances. All judicial litigation, including confiscations based on non-convictions, should, in principle, be made public. A sufficient justification must be found to depart from the principle of publicity even though confiscation proceedings deal with a civil matter, namely the legality of the funds. A public hearing contributes to achieving Article 6 (1), a fair trial, by making the administration of justice visible. It is essential to consider that the State or State agency is a party to the proceedings and that confiscation leads

14 *Beyeler v. Italy* [GC], no. 33202/96, §§ 109–10, ECHR 2000-I and *Lekić v. Slovenia* [GC], § 97.

15 *Markus v. Latvia*, no. 17483/10, 11 September 2020.

16 *Kilin v. Russia*, no. 10271/12, 11 August 2021.

to material gain for the State. For this reason, only limited exceptions can be made for public hearings. Otherwise, property owners' rights might be violated by arbitrariness and administration of justice in secret without public scrutiny, which could violate their right to a fair trial.

4. Equality Before the Law
   The rule of Law also embodies the principle of equality before the law. This principle means that the law must ensure that no discrimination is allowed based on race, colour, sex, language, religion, political opinion, nationality, country of origin, or birth.
5. Access to Justice
   Access to justice is another principle emanating from the rule of law. Access to justice implies the presence of an independent and impartial judiciary to achieve the classical formula: "Justice must not only be done but also seen to be done".

6 Legitimate Aim in the General Interest

Having established that the State has only the right to interfere if the law permits it, the second principle to consider is that any interference must be justified for the benefit of the public. Therefore, the State may only interfere with the peaceful enjoyment of property if it also serves a legitimate public interest.

According to the ECHR, public and general interest are used interchangeably, but the Convention does not define such a concept.[17] The ECtHR has only stated in these past seven years that it means "public concern warranting measures to be applied".[18] Legal writers further clarified that the "public interest" test is satisfied if the confiscation seeks to prevent "the illicit use, in a way dangerous to society, of possessions whose lawful origin has not been established".[19]

However, irrespective of the definition adopted to such a term, and even before it defined the term public interest, the ECtHR consistently maintained, at least for the past thirty years, that confiscating criminal property was in the public interest.[20] The ECtHR further established in ***Raimondo v. Italy***[21] that protecting the general interest is not a criminal sanction but a preventive

17 *Lekic v Slovenia*, no. 36480/07, 14 February 2017.

18 *Ibid.*

19 Sofia Milone, "On the Borders of Criminal Law. A Tentative Assessment of Italian Non-Conviction Based Extended Confiscation", *NJECL* 8, no. 2, 2017, pp. 150–170.

20 *Raimondo v. Italy*, 22 February 1994, § 30, Series A no. 281A.

21 *Ibid.*

measure, thus fulfilling the legitimate aim of protecting the general interest. In ***Todorov and Others v. Bulgaria***,[22] the ECtHR also stressed that confiscating money or assets obtained illegally or purchased with proceeds of crime was a necessary and effective means for combating crime.

7 Proportionality of a Confiscation Measure

After defining lawfulness and the general interest, one must consider the proportionality principle when safeguarding the general interest. Accordingly, Protocol No. 1 requires any interference to be reasonably proportionate to the goal sought. To effectively challenge the measures interfering with the rights guaranteed under this provision, the individual must also be given a reasonable opportunity to present their case to the competent authorities in judicial proceedings concerning the right to peaceful enjoyment of one's possessions. However, Protocol No. 1 provides no explicit procedural requirements in Article 1.

Case law, however, shows that proportionality can be subjectively defined and can tremendously change from one society to another. The ECtHR usually allows national states to determine the fulfilment of the proportionality test. In ***Lekic v. Slovenia***,[23] the ECtHR said that the national authorities know best "because of their direct knowledge of their society and its needs". In fact, for instance, the Court in ***Raimondo v. Italy***[24] concluded that confiscations in mafia cases were an effective weapon against organised crime. The ECtHR again recalled in ***Gogitidze and Others v. Georgia***[25] that civil proceedings *in rem* are proportionate to the State's efforts to combat criminality.

In recent decades, however, the ECtHR has also stated that proportionality can be met if public authorities use less intrusive measures to combat criminality.[26] Consequently, the ECtHR gives conflicting judgements when national authorities can act independently and when their methods are inappropriate. Furthermore, the ECtHR has never explicitly stated how such less intrusive measures can be implemented. Accordingly, although the ECtHR held that confiscation measures were proportionate in the above cases, it ruled against them in other cases. In ***Rummi v. Estonia***,[27] the ECtHR determined in

22 *Todorov and Others v. Bulgaria*, nos. 50705/11 and 6 others, para. 189, 13 July 2021.
23 *Lekic v. Slovenia*, no. 36480/07, 14 February 2017.
24 *Raimondo v. Italy* (n. 20).
25 *Gogitidze and Others v. Georgia*, no. 36862/05, 12 May 2015.
26 *James and Others v. United Kingdom,* § 51; *Koufaki and Adedy v. Greece* (dec.), § 48.
27 *Rummi v. Estonia*, no. 63362/09, 22 November 2009.

2015 that the confiscation order was disproportionate since no criminal activity was connected to the confiscated property. The ECtHR reached the same conclusion in 2021, whereby in its most recent case, ***Todorov and others***,[28] the ECtHR analysed non-conviction-based confiscation in detail, contending that forfeited assets must be linked to alleged crimes. In this case, the domestic courts did not establish a link between the applicant's criminal conduct and the forfeited assets; instead, they relied on the presumption that the assets were proceeds of crime. The ECtHR contended that the domestic courts failed to indicate whether forfeited assets equalled the discrepancy between the applicants' income and expenditures.

8 Applicability with Article 6

The ECtHR also stipulates that confiscations not based on conviction must align with Article 6 of the ECHR when it determines that the State is entitled to interfere to prevent criminality. The provisions of this article govern both civil and criminal proceedings.

In ***Engel and Others v. the Netherlands***,[29] the ECtHR outlined criteria for evaluating which part of Article 6 of the ECHR can apply to non-conviction-based confiscations. It determined that the specific and independent criteria to determine whether such confiscation is criminal or otherwise are the following: (a) the legal classification of the offence under national law, (b) the essential nature of the offence, and (c) the nature and severity of the consequences to which the respondent is subjected.[30] The second and third criteria are alternative and not cumulative. This paper shall demonstrate that, as the ECtHR observes, a confiscation model without a conviction is outside the criminal sphere and does not have to adhere to the stricter rules stipulated in Articles 6 (2) and 6 (3) of the ECHR and Article 6 (1) shall apply.

9 The Legal Classification of the Offence under National Law

The ECHR does not define "criminal charges" in practice. The ECtHR simply stated in 1980 in ***Deweer v. Belgium***[31] that the "charge", contemplated by Article 6, is taken as "substantive", as opposed to "formal", and it "could … be defined

28 *Todorov and Others v. Bulgaria* (n. 22).

29 *Engel and Others v. the Netherlands*, 8 June 1976, paras. 82–83, Series A no. 22.

30 *Ibid.*

31 *Deweer v. Belgium,* 1980, § 44.

as the official notification given to an individual by the competent authority of an allegation that he has committed a criminal offence", a definition that also corresponds to the test whether "the situation of the [suspect] has been substantially affected".[32]

In these past four years, the ECtHR has gone one step further by stating that it is crucial to examine national law to determine whether an offence is criminal.[33] The ECtHR clarified in ***Jónsson and Ragnar Halldór Hall v. Iceland*** [GC][34] that this would be decisive if domestic law classifies an offence as criminal. Otherwise, the ECtHR contemplated that the national court must look behind the national classification and examine the substantive reality of the procedure.[35]

Having said this, the ECtHR repeatedly ruled that confiscation orders are not criminal charges since they are preventive measures, as outlined under Article 1 Protocol 1. As a result, civil law rules apply.

10 The Essential Nature of the Offence

A law may decide whether an offence is criminal, but categorisation alone is insufficient. A closer look at the real nature of the offence is paramount to understanding whether it is criminal in nature.

The ECtHR interpreted this second criterion as not violating Article 6 under its criminal heading if the confiscation proceeding was initiated independently of a finding of criminal activity or guilt of specific offences, did not involve any allegations of criminal behaviour, and was not ancillary or dependent on any criminal prosecution or conviction.[36]

11 The Nature and Severity of the Consequences to Which the Respondent Is Subjected

The ECtHR regards a confiscation order under non-conviction-based confiscation as recovering assets lawfully not belonging to the respondent. Therefore, this confiscation order serves as a non-punitive penalty designed to deter people from engaging in crime and to keep the proceeds from being used

32 *Ibid.*, §§ 42 and 46 and *Eckle v. Germany,* 1982, § 73.
33 *Gestur Jónsson and Ragnar Halldór Hall v. Iceland* [GC], 2020, §§ 85 and 77–78.
34 *Ibid.*
35 *Ibid.*
36 *Benham v. the United Kingdom*, 1996, § 56.

in the future.[37] As the ECtHR clarified, confiscating property ordered without a criminal charge is not punitive but preventive and compensatory and thus cannot cause the application of Article 6 (2).

12 The EU and International Organisations

The EU and numerous international organisations also find difficulty in drawing a line to explicitly state that non-conviction-based confiscations are purely civil, as they also appear to link the property with criminal offences for that property to be confiscated since the first thought of including these types of confiscations in the 1990s. Legislators began considering non-conviction-based confiscations in the 1990s when these international organisations started providing guidelines, but have only provided them without interfering with countries' non-conviction-based confiscations. The EU and international organisations only appear to identify the need to enact legal provisions to combat criminality without stating how or when the provisions should be enacted. As a result, the EU and international organisations may also determine that the four models mentioned above could be risky, as they may violate human rights if implemented.

The Strasbourg Convention, an initiative by the Council of Europe 1990, proclaimed that one of the "modern and effective methods" in the "fight against serious crime … consists in depriving criminals of the proceeds from crime".[38] Specifically, the Convention called on the signatory states to adopt legislation and other measures to enable it to confiscate instrumentalities, proceeds, or property whose value corresponds to the proceeds.

Ten years passed before the enactment of the United Nations Convention against Transnational Organised Crime (Palermo Convention) in 2000. In paragraph one of Article 12, this Convention stated that the States must adopt, to the greatest extent possible within their domestic legal systems, measures that may be necessary to confiscate proceeds of crime derived from criminal offences or property the value of which corresponds to such proceeds. The burden of proof for the offending parties is reversed in paragraph eight, where they must show the lawful origin of the confiscated property or proceeds of crime.[39] However, Article 54 of the Convention states that each State Party

37 *Gogitidze and Others v. Georgia* (n. 25) and *Todorov and Others v. Bulgaria* (n. 22).

38 Council of Europe, 'Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime', 1990, <168007bd23 (coe.int)> accessed 27 March 2024.

39 United Nations on Drugs and Crime, ' United Nations Convention Against Transnational Organised Crime and the Protocols Thereto', 2004, <UNITED_NATIONS_CONVENTION_AGAINST_TRANSNATIONAL_ORGANIZED_CRIME_AND_THE_PROTOCOLS_THERETO.pdf (unodc.org)> accessed 27 March 2024.

may confiscate such property without criminal convictions in cases where the offender cannot be prosecuted due to death, flight, absence, or other appropriate circumstances. The United Nations Convention Against Corruption also provides for a similar provision.[40]

Soon after the year 2000, the Warsaw Convention was enacted in 2008, which updated the Strasbourg Convention of 1990. Under Article 3 (1), each Party has the right to confiscate instrumentalities and proceeds or property whose value relates to such proceeds and laundered property. Implementing the Warsaw Convention is considered a key component of preventing and repressing organised crime because "to date, the Warsaw Convention remains the only comprehensive treaty covering both the prevention and repression of money laundering, as well as financing of terrorism, recovery of proceeds of crime, and international co-operation. Its unique features include being the only international treaty that grants national authorities the power to halt suspicious transactions at the earliest stage and to prevent their movement through the financial system".[41]

In 2012, the Financial Action Task Force (FATF) provided that "Recommendation 4 states that countries should consider adopting measures that allow laundered property, proceeds or instrumentalities to be confiscated without requiring a criminal conviction (non-conviction based confiscation) to the extent that such a requirement is consistent with the principles of their domestic law".[42]

The EU has also taken the stance that non-conviction-based confiscation shall be limited to when there is a link with criminal activities. In fact, "in a resolution on organised crime, corruption and money laundering from June 2013, the Parliament invited Member States to consider implementing models of civil law asset forfeiture. Such a possibility was to be restricted to cases where, on the balance of probabilities and subject to the permission of a court, it could be established that assets are the result of, or are used for criminal activities".[43]

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40 United Nations on Drugs and Crime, 'United Nations Convention Against Corruption', 2004, <UN_Convention_Against_Corruption.pdf (unodc.org)> accessed 27 March 2024.

41 Ioannis Androulakis, 'Recovery of Proceeds from Crime – Time to Upgrade the Existing European Standards?', 2023, <Recovery of Proceeds from Crime – Time to Upgrade the Existing European Standards? – eucrim> accessed 27 March 2024.

42 Financial Action Task Force, 'Best Practices on Confiscation (Recommendations 4 and 38) and a Framework for Ongoing Work on Asset Recovery', October 2012, <Best Practices on Confiscation and a Framework for Ongoing Work on Asset Recovery.pdf (fatf-gafi.org)> accessed 26 March 2024.

43 European Parliament, 'Legislative Train 08.2, 7 Area of Justice and Fundamental Rights / Up to €7BN, Common Rules for Non-Conviction Based Confiscation', <report (europa.eu)> accessed 26 March 2024.

The Council of Europe also confirmed in 2020 that "NCB proceedings represent an important weapon in the fight against illicit property and are gaining increasing recognition as a way forward. The alignment of any system with Convention rights will be case-specific, but, in principle, there is no incompatibility. However, for an NCB framework to be effective and fair, judicial oversight is the touchstone. Provisions must clearly define the scope of property, enable the swift restraint of assets and asset-tracing, recognise orders made overseas and provide for respondent and third-party participation. No doubt, the crafting of a lasting NCB framework requires careful planning and robust debate. Once introduced, however, it can be a mighty tool against dirty wealth".[44]

Besides the fact that the EU and international organisations always seem to link non-conviction-based confiscations with criminal offences to avoid infringements of individuals' human rights, they also seem to have repeatedly spoken in terms of certain specific categories of crimes only. Indeed, the Strasbourg Convention refers to serious crimes without specifying what they are. The subsequent enacted Conventions or opinions always mentioned transnational crimes or corruption. Transnational organised crimes refer to "virtually all serious profit-motivated criminal actions of an international nature where more than one country is involved".[45] However, there may also be other international crimes, such as theft or fraud, that may only happen in a particular country. Despite being an offence in all countries, theft does not always fall under the transnational crime category since only one country may be involved in that particular scenario[46], with the result that the EU and international organisations do not seem interested in regulating these offences as well.

13 Problems with Non-Conviction-Based Confiscations

The *Engel* criteria established that civil procedural laws apply to confiscations without conviction, and the national authorities must present evidence according to civil rules. In many cases, the attempts to characterise the non-conviction-based confiscation as criminal have failed in the ECtHR.[47]

44 Council of Europe (n. 1).

45 United Nations Office on Drugs and Crime, 'Transnational Organized Crime – The Globalized Illegal Economy', <TOC12_fs_general_EN_HIRES.pdf (unodc.org)> accessed 26 March 2024.

46 LibreTexts, Social Sciences, 13.1: International Crime or Transnational Crime? Some Definitions', <13.1: International Crime or Transnational Crime? Some Definitions – Social Sci LibreTexts> accessed 26 March 2024.

47 *Walsh v. the United Kingdom* (striking out), no. 33744/96, 4 April 2000, *Saccoccia v. Austria,* 18 December 2008, no. 69917/01, *Gogitidze and Others v. Georgia*, no. 36862/05, 12 May

Nevertheless, lowering the bar of evidence required to prove that the respondent has property that should be confiscated would inevitably lead to human rights violations due to the speed at which the national authorities could prove their case without being sure that what they were proving was correct. The following sections will examine two civil procedural laws to illustrate why categorising confiscations as civil can be problematic.

14 Presumption of Innocence

As a general rule, the presumption of innocence applies to criminal proceedings, which implies that the prosecution has the burden of proving beyond reasonable doubt that the accused committed the offence. Nevertheless, realistically, the presumption of innocence is intertwined with the burden of proof, even when dealing with civil cases, where it is an uncontested principle that those making allegations must establish them. Wilkinson III also embraces this concept and shows through the historical overview of such principle how the presumption of innocence cannot be ignored in civil cases.[48] Uzelac and Rhee further argue that "This aspect of Article 6(2) is applicable in civil cases, for instance, when a court orders a person to pay compensation because of an action of which he has previously been acquitted in a criminal case. Acquittal in the criminal case does not preclude civil liability, but the presumption of innocence might be infringed if the civil judgment includes a statement imputing criminal liability".[49] Thus, they argue that the presumption of innocence and the burden of proof cannot be ignored and must be applied rigidly whenever the civil case might be linked to criminal charges.

These two principles must be paired with the right to adversarial proceedings, which means that all parties shall have the opportunity to have knowledge of all evidence presented and to comment on it if they choose. Disregarding a fundamental principle as the right to adversarial proceedings to save time and expedite the process is unjustified. Unless the State strictly adheres to this rule, it may be in a position to violate the procedural rights of the property owner. The ECtHR shall evaluate whether the applicant had a reasonable opportunity

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2015, *Butler v. UK* (*dec.*), 27 June 2002, no. 41661/98, ECHR 2002-VI., *Zschüschen v Belgium*, no. 23572/07, ECHR 178 (2017).

48 J. Harvie Wilkinson III, 'The Presumption of Civil Innocence', Virginia Law Review, June 2018, Vol. 104, No. 4 (June 2018), pp. 589–653, <https://www.jstor.org/stable/44863413> accessed 25 March 2024.

49 M. Strandberg, The Presumption of Innocence in Civil Cases from Fundamental Procedural Rights from a National Angle (1st edn., Cambridge University Press 2018).

to present his arguments before the domestic courts, considering that it had a comprehensive view of the case. Consequently, the confiscation procedure cannot be marred by manifest arbitrariness and conflict of interest if the applicant can present his case and make arguments before the domestic court. When considering ***Rummi v. Estonia***,[50] the ECtHR said it could not see how property obtained through crime could be confiscated. The ECtHR viewed the confiscation as arbitrary, resulting from somewhat incidental evidence seizures. The ECtHR noted that the confiscation of particular assets did not appear to have been based on a detailed assessment. It was also impossible for the applicant to challenge the opposite side meaningfully and present a case. Accordingly, the judicial proceedings had been deficient, violating Article 6(1).

Unfortunately, national courts, many times blessed by the ECtHR, have pushed the presumption of innocence, the burden of proof and the right to adversarial proceedings to the limit by stating that a confiscation based on non-conviction can shift the burden of proof from the prosecution to the owner. However, given the nature of these confiscations, it is not entirely clear that the presumption of innocence can be discarded, and the burden of proof can be shifted without violating human rights.

Considering these argumentations, the ECtHR clarified that shifting the burden of proof is permissible if "exceptional" circumstances exist,[51] but without ever clarifying when exceptional circumstances occur but only examining every case on an individual basis that can result in subjective results. Such subjectivity can be observed in ***Telbis and Viziteu v. Romania***.[52] This case involved an official who had committed 291 acts of bribery over an extended period. The ECtHR accepted the justification for extended confiscation based on the need to "prevent and eradicate corruption in the public service". The ECtHR concluded that the applicant's family had acquired substantial estates disproportionate to their lawful income in a relatively short time. As the applicant was presumed to have benefited unduly from the proceeds of his crimes, it was reasonable to expect them to satisfy their burden of proof by refuting the prosecutor's substantiated suspicions about the wrongful origins of their assets. The ECtHR reiterated the same subjective conclusion in ***Grayson and Barnham v. the UK***,[53] ***Butler v. the UK***,[54] ***Gogitidze and Others***[55] and ***Phillips v. the UK***.[56]

50 *Rummi v. Estonia*, (n. 27).
51 *Silickienė v. Lithuania*, no. 20496/02, paras. 67–69, 10 April 2012.
52 *Telbis and Viziteu v. Romania*, no. 47911/15, 26 June 2018.
53 *Grayson and Barnham v. the UK*, no. 19955/05 and 15085/06, 23 September 2008.
54 *Butler v. the UK*, no. 41661/98, 27 June 2002.
55 *Gogitidze and Others v. Georgia* (n. 25).
56 *Phillips v. the UK*, no. 41087/98, 12 December 2001.

15 Evidence Presented

The burden of proof in conviction cases shall be beyond a reasonable doubt. However, in non-conviction cases, the parties shall present their case based on probability. The ECtHR discussed this principle in ***Zschüschen v. Belgium*** in 2017.[57] In this case, the plaintiff opened a Belgian bank account and deposited substantial money in five instalments. The bank reported this fact, and criminal proceedings were initiated against the plaintiff. Ultimately, the court issued a confiscation order against the deposited money because the court noted that the plaintiff failed to explain how he got the money. Therefore, the ECtHR concluded that national courts did not need proof "beyond reasonable doubt" of the illicit origins of property confiscated through civil proceedings *in rem* that related to proceeds of crime obtained from criminal offences. The proportionality test was instead based on a balance of probabilities or a high probability of illicit origins combined with the inability to prove otherwise.

Two years later, the ECtHR adopted the same rationale in ***Balsamo v. San Marino***,[58] where it found that the relevant domestic authorities could issue confiscation orders based on a preponderance of evidence that the respondents' legal incomes would not have been sufficient for them to acquire the property in question.

16 Considerations on the above Analysis

The paper demonstrates that although crime must not pay in principle, national authorities must take all necessary steps to ensure that individuals' rights are not violated. The above discussion suggests that civil non-conviction-based confiscation is not a human rights violation so long as clear measures are adopted. According to the first three models examined above, non-conviction-based property confiscation is linked to criminal activity. Therefore, as long as the proceeds are linked to the criminal offence, the State is free to confiscate that property, as it is necessary to demonstrate that crime does not pay. Thus, it seems justified and in line with human rights protection to allow confiscations in this case when the accused absconds or dies before the criminal proceedings are completed, according to the ECtHR's rationale, regardless of whether the property is owned by the owner or by a third party. The State must prove to society that it is doing something to ensure crime does not pay. Removing

57 *Zschüschen v Belgium*, no. 23572/07, ECHR 178 (2017).

58 *Balsamo v. San Marino*, nos. 20319/17 and 21414/17, 8 October 2019.

the criminal element from confiscation seems understandable in these exceptional circumstances because obtaining a criminal conviction is impossible.

However, it appears difficult to state that non-conviction-based sanctions are civil and that civil procedural law applies for one main reason, even though the legislator's intention in some countries seems justified on the principle that crime does not pay. National courts, along with the ECtHR, allowed subjectivity to get the best of them and were only sometimes consistent in justifying the application of non-conviction-based confiscations, stating that all countries are unique and different approaches should be based on their cultures. Indeed, in ***Lekic v. Slovenia***,[59] the ECtHR said that the national authorities know best "because of their direct knowledge of their society and its needs". For instance, the fight is against organised crime in Italy, and no other offence seems as important. The ECTHR stressed that "the organised crime phenomena in Italy reached an alarming scale. The Mafia-type groups are so widespread that, in some areas, the authority of the State is significantly weakened. The large profit gained through illicit activity confers a power upon them, which undermines the primacy of the law in the State. As a consequence, the means employed to fight such an economic power such as the preventive confiscation seems to be crucial to effectively tackle those groups".[60] However, at the same time, among various cases, in 2015, in the case of ***Rummi v. Estonia***,[61] the ECtHR concluded that confiscation was disproportionate, as there was no link between the confiscated property and any crime, regardless of the society's background.

Also, adopting the fourth model of non-conviction-based confiscation is problematic since countries that use this method allow discretion when undeclared wealth orders are to be applied. Countries have used their reasonable grounds of belief without specifying exactly what evidence to examine or how to do so when determining when to apply this order. Kenya, for example, does not require any amount to be exceeded to trigger the order. In contrast, Mauritius requires US$227,800 in cash or MUR 2.5 million (US$57,000) in bank deposits.[62]

59 *Lekic v Slovenia*, no. 36480/07, 14 February 2017.

60 Open-ended Intergovernmental Working Group on Asset Recovery, *'The Italian experience in the management, use and disposal of frozen, seized and confiscated assets'*, 2 September 2014, <Combined_CacCosp-Wg2-2014-CRP3.pdf (unodc.org)> accessed 25 March 2024.

61 Rummi v. Estonia, (n. 27).

62 Jean-Pierre Brun et al., *Unexplained Wealth Orders: Toward a New Frontier in Asset Recovery*, June 2023 <StAR-wealth-report-08.pdf (worldbank.org)> accessed 26 March 2024.

17 Way Forward

Based on the above analysis, five crucial factors must be addressed to progress. The first point is that the ECtHR must maintain its position that all non-confiscation-based models are civil and do not violate Articles 6(2) and (3). The models cannot be deemed criminal because there can never be a conviction in certain circumstances, such as death or abscondment. Since this conviction will never be achieved, declaring the confiscations criminal would be misused.

Second, the ECtHR must declare once and for all that human rights cannot be violated regardless of what model the State adopts to combat crime. It must ensure that it allows States to work in the best interest of their society without determining that, in one case, the State decided correctly whilein another case, it will discuss that the proportionality principle was not reached, and the State in question would have violated the individual's human rights. Such uncertainty may make State officials uncomfortable implementing all of the non-conviction-based confiscation models discussed above if conflicting cases continue to be delivered.

Third, legislators must come together and take one approach to combat criminality, as legislators must embrace the need to enact unequivocal laws that allow for applying all four models of non-conviction-based confiscation. As a starting point, legislators in all countries must identify which provisions work best and then enact one law to ensure that all persons face the same consequences worldwide and do not shop for jurisdictions. Countries must together decide the thresholds, if any, to apply to trigger undeclared wealth orders, and they should also apply to all property within its jurisdiction, regardless of its owner's nationality. The author recognises, however, that political will is required from all parties, namely international organisations, the EU, and individual States.

The fourth point is that shifting the burden of proof is against all principles applicable to criminal and civil cases. It is, therefore, essential to maintain the presumption of innocence without undermining the fight against criminality. The burden of proof, however, must be based on probabilities after applying a reasonable approach. The prosecution can fulfil such a requirement of this burden of proof by, for example, presenting the tax papers a person has filed and the property the person holds to determine whether the person is guilty of illicit enrichment, thereby ensuring an effective method to combat illicit enrichment so that an undeclared wealth order can be issued to confiscate such property. As a result, individuals alleging that other persons have acquired property by illicit means must calculate how much they have accumulated over and above what has been declared to have the property confiscated.

As a final and fifth point, the person who decides to reply to such an undeclared wealth order must not be criminally prosecuted, as in Kenya, because that would violate their human rights.

18 Conclusion

Bulgaria, Czech Republic, Greece only for tax evasion, Ireland, Latvia, Lithuania, Netherlands, Portugal, Romania,[63] and Australia[64] have enacted laws covering all four non-conviction-based confiscation models. More countries must follow suit to ensure that the fight against criminality is successful in the long run, resulting in the States protecting society. Transnational crimes alone generate trillions of dollars each year,[65] indicating that States must act together and do more to combat criminality effectively. Based on the results of this study, non-conviction-based confiscation efforts are needed to protect society, whose rights must extend beyond an individual's criminal rights.

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65 Global Financial Integrity, 'Transnational Crime', 2004, <Transnational Crime (gfintegrity.org)> accessed 29 March 2024.

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CHAPTER 15

Creating Criminal Law Rules at the EU Level

Stefano Filletti

Abstract

In this chapter, the author analyses how, over time, the European Member States have ceded national sovereignty to the European Union, where particular areas of criminal law are concerned. The progress made in the creation of a quasi-federal Europe for criminal law is the fruit of a struggle between Member States, on the one hand, seeking to retain their national sovereignty, and on the other hand, recognising the need to face reality, this being that European criminality does not stop where national physical territories end, but seeks to take advantage of the borderless Europe. That same borderless European Union requires a system to match to effectively combat criminality and maintain an area of freedom, security and justice in which the European Citizen can prosper.

1 Introduction

The Area of Freedom, Security, and Justice (AFSJ) within the European Union (EU) has evolved significantly. One crucial aspect of this development has been establishing an identifiable EU criminal territory. This article delves into the challenges faced during this journey, Member States' resistance to retaining sovereign control over criminal law matters, and the legal developments that shaped the landscape.

As the EU sought to create a cohesive criminal justice framework, it encountered numerous obstacles. Member States were understandably protective of their national legal systems and hesitant to cede authority to supranational institutions. The tension between harmonisation at the EU level and the preservation of state sovereignty posed a formidable challenge.

Two distinct streams emerged during this process. On the one hand, Member States engaged in discussions regarding harmonising rules and mutual assistance mechanisms. Efforts were made to align legal norms across borders, ensuring consistency in criminal procedures and cooperation in investigations. Simultaneously, Member States recognised the need to tackle transnational criminal networks effectively. Collaborative efforts led to the creation

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of European agencies, enhanced investigative procedures, and the adoption of mutual recognition instruments.

The European Arrest Warrant (EAW) and the European Investigation Order (EIO) are pivotal achievements. These instruments facilitate swift cross-border cooperation, allowing for the arrest and extradition of suspects and the exchange of evidence. They bridge the gap between national legal systems and contribute to developing EU criminal norms.

This article explores the delicate balance between these two realities—the drive for harmonisation and the imperative to combat organised crime. By examining legal developments within this context, we gain insights into how the EU's criminal justice landscape has evolved. Ultimately, both harmonisation efforts and practical cooperation have contributed to establishing an identifiable EU criminal territory.

2 The Humble Origins of the European AFSJ

A proper criminal law structure requires an identifiable physical territory whereby penal norms may be applied. When considering the European Union against such a backdrop, it becomes evident that the European Area of Freedom, Security and Justice (AFSJ) *prima facie* aligns with the notion of 'territory'. Therefore, an examination from a legal standpoint as to whether or not the AFSJ may be regarded as constituting a 'territory' to apply penal norms at the EU level becomes necessary. At its inception, the AFSJ was geared towards establishing a zone whereby a series of common norms, including *inter alia* criminal norms, may be applied across the area. In this respect, reference should be made to Article 3(2) of the consolidated TEU post-Lisbon, whereby express reference is made to preventing and combatting crime within the Union by virtue of appropriate measures.

The powers to legislate, enforce and sanction, respectively, have long served as distinct, identifiable criteria of sovereignty in international law.[1] Whilst Member States have undeniably retained their national sovereignty over their national territories, a thorough appreciation of the AFSJ sheds light on the fact that a degree of sovereignty has indeed been bequeathed to the European Union. Indeed, the European Union is afforded a degree of power to legislate, enforce and create sanctions in relation to those offences established within the respective territory, as delineated by the AFSJ.

1 Mills A., Rethinking Jurisdiction in International Law, British Yearbook of International Law (2014), OUP, 2014.

The origins of the AFSJ may be traced back to the Trevi meeting,[2] whereby an agreement was reached among States to undertake cooperation efforts in curbing terrorism and organised crime, which indirectly led to the inception of a series of agencies at the European level, such as Europol and Eurojust, *inter alia*. Another notable milestone was achieved at Tampere,[3] whereby an agreement was reached among Member States towards undertaking judicial and investigative cooperation efforts throughout the European Union. At the same time, positive strides towards improving the mutual recognition of judgements were also made. The Trevi meeting was of paramount importance in ensuring that the AFSJ developed on concrete foundations, simultaneously also paving the way for further enhancements within the realm of substantive criminal law.

Within this context, it becomes appropriate to highlight the significance of the Treaty of Amsterdam and the Meeting at The Hague in reinforcing and enhancing the approximation of criminal law and strengthening particular agencies, such as Eurojust and Europol, while promoting and enhancing cooperation and mutual recognition among Member States. The elimination of border restrictions and obstacles further aided in strengthening the AFSJ.

Based on the approximation of criminal law, the Council Framework decisions enabled states to create similar norms and achieve similar results within the criminal law area. This allowed for a true area of cooperation and justice

2 TREVI intergovernmental group, setup during the **European Council** Summit held in **Rome**, 1st and 2nd December, 1975, subsequently merged with the Justice and Home Affairs pillar with the Treaty of Maastricht, 1992.

3 The European Council held a special meeting on 15 and 16 October 1999 in Tampere on the creation of an area of freedom, security and justice in the European Union. Salazar L., in *Twenty Years since Tampere, The Development of Mutual Recognition in Criminal Matters, EUCRIM, 2020, issue 4/2019* best described the Tampere conclusions as follows: "… the Tampere Conclusions dealt with all the traditional matters of Justice and Home Affairs: "Asylum and Immigration, Civil and Criminal Justice, Fight against Crime and External Policy". Under the chapter entitled "A Genuine European Area of Justice", together with the subjects of access to justice and convergence in civil law matters, special attention was devoted to mutual recognition of judicial decisions. Under point 33 of the Tampere Conclusions, after having affirmed that cooperation between authorities and the judicial protection of individual rights would be facilitated by enhanced mutual recognition of judicial decisions and judgements and the necessary approximation of legislation, the European Council endorsed the principle of mutual recognition as "the cornerstone of judicial cooperation in both civil and criminal matters within the Union", which should apply both to judgements and to other decisions of judicial authorities".

within the EU context, allowing Member States to achieve common goals and results. This evolution paved the way for the Stockholm Programme.[4]

In tracing the way forward, the Stockholm Programme[5] is of key interest. It aims to establish a new agenda for the AFSJ, focusing on substantive and procedural aspects of EU criminal law, approximation, mutual recognition, and introducing new concepts such as minimum defence rights. The Justice & Home Affairs Council[6] more recently highlighted the importance of consolidating existing instruments, enhancing procedural guarantees, and combating fraudulent behaviour and immigration issues, which concerns were also voiced in the Treaty of Lisbon. Notably, it also established an office of the European Public Prosecutor, a landmark achievement.

Both the AFSJ and EU Criminal Law respectively developed by virtue of numerous elements, including *inter alia* factual realities, intergovernmental dialogue and the constitutional organisation of the European Union. Furthermore, the thorough constitutional reform of the Union was cemented by virtue of the elimination of the 'pillars' structure, which Lisbon undeniably spearheaded. The Union's novel formulation facilitated a series of widespread developments that ran parallel to and mirrored the Member States' desire to enhance criminal law at the European Union level, a desire manifestly evidenced by the Stockholm Programme.

Constitutional developments within the Union impacted both the AFSJ and national legislation. Indeed, the applicability of norms at the Union level became more significant by virtue of a series of normative constitutional developments in the EU. Furthermore, such developments meant that the direct effect of EU norms on national law became even stronger. Notably, domestic legislation which ran counter to established Union rules could also be rendered inapplicable, leading to the well-known notion of judicial review. In seeking to appreciate the direct and indirect impact that rules pertaining to

4 The Stockholm Programme sets out the European Union's (EU) priorities for the area of justice, freedom and security for the period 2010–14. Building on the achievements of its predecessors the Tampere and Hague programmes, it aims to meet future challenges and further strengthen the area of justice, freedom and security with actions focusing on the interests and needs of citizens. In order to provide a secure Europe where the fundamental rights and freedoms of citizens are respected, the Stockholm Programme focuses on the following priorities: Europe of rights; Europe of justice; Europe that protects; Access to Europe; Europe of solidarity; Europe in a globalised world, *vide* OJ C 115, 4.5.2010, pp. 1–38.

5 See also *Strategic Guidelines for the Next EU's Justice and Home Affairs Programme: Steady as she Goes*, 13th Report of Session 2013–2014, European Union Committee, House of Lords, UK.

6 Meeting 5–6 June 2014. See also *The Stockholm Programme* in *EUCRIM*, 2014/2, Max-Planck Institute, 2014, p. 47.

criminal law have had *vis-à-vis* domestic legislation, it is imperative to comprehend and thoroughly appreciate the constitutional developments in both the AFSJ and the Union.

3 National Reluctance to Cede Sovereignty

What follows is a historical overview of the AFSJ's development, demonstrating how the development of penal norms at the Union level has occurred while simultaneously explaining the rationale behind the traditionalist stance adopted by Member States when assenting to criminal law rules at the European Union level.

When negotiating the EC Treaty,[7] States debated whether criminal law should be included in the Community's competence. As a result of these negotiations, the Single European Act was established. Since political will at that time tended to favour limiting the development of criminal law at the European level, States were willing to restrict cooperation to specific situations such as extradition and surrender of individuals and serious transnational organised crime. Indeed, discussions about a common justice and home affairs system for Member States were hotly contested and opposed.[8] Despite recognizing that certain matters should or could be addressed at a supranational Union level, States believed that judicial and police cooperation should remain intergovernmental. Maastricht[9] introduced a three-pillar structure for the EU as a compromise.

4 The Creation of the 'Pillar' System of Cooperation

The EU's three pillars were designed to distinguish between the various types of cooperation developed within it. They reflected the disposition of the Member States *vis-à-vis* the cession of national sovereignty was concerned. The different forms depended on the policy area and the relevant Treaty provisions. Cooperation at the first pillar stemmed from the EC Treaty and the EU's

7 Treaty Establishing The European Community, 24 December, 2002, OJC 325.

8 See also S. Carrera and F. Geyer, "The Reform Treaty and Justice and Home Affairs: Implications for the Common Area of Freedom, Security and Justice", in E. Guild and F. Geyer (eds), Security versus Justice? Police and Judicial Cooperation in the European Union, Ashgate: Hampshire, 2008.

9 The Treaty on European Union was signed in Maastricht, 1992.

ability to promulgate legislation which directly binds Union citizens. The first pillar finds the Customs Union, Economic Monetary Union, Internal Market, and agricultural and trade policies at the supranational level. The second pillar dealt with common foreign and security policy, and the third pillar, concerning police and judicial cooperation, relied on intergovernmental cooperation.

Essentially, Maastricht provided a basis for criminal justice and police cooperation by delegating them to the third pillar but restricted any progress to unanimous agreement. In the Treaty, cooperation and collaboration between States were enshrined as key elements. As part of the Treaty, a Coordinating Committee was also established to assist in the preparation of Council discussions and to provide opinions to the Council. As a result, the prevailing state of affairs at the time was largely consolidated and crystallised. When a unanimous agreement was achieved, the Council could take the initiative and action concerning matters pertaining to the third pillar. Whilst this power of the Council constituted a notable development permitting institutional impetus, such power was merely cosmetic with limited substance precisely because a unanimous agreement between Member States was rarely achieved.

Against this backdrop, it is worth mentioning a series of Conventions, including *inter alia* the Convention of 1995 on the Protection of the EC financial interests[10] and its Protocols[11] and the Convention of 1997 on the Fight against Corruption involving Officials of the EC or Officials of the Member States of the EU.[12] The issue that manifested itself here was that unanimity amongst Members was first necessitated for such conventions to come into force. If this was not enough, subsequent ratification by Member States was also necessary. These legal obstacles made the approval of Conventions a rather challenging task. This is further evidenced by the fact that only one Convention was concluded within the third pillar framework, namely the Europol Convention of 1995.[13]

In this respect, reference must be made to Joint Action plans, which, to some extent and in a similar fashion to the so-termed 'common positions', became a norm.[14] Such joint actions were taken in adopting action plans or setting our particular operations and were binding on all Member States. These 'common positions' referred to declarations that identified the Union's position on

10 Drafted by Council Act of 26 July 1995 OJ C 316, 27.11.1995.

11 Protocol 1 came into force on 17/10/2002. The second protocol came into force on 19/5/2009.

12 OJ C 195 of 25 June 1997.

13 European Police Office, OJ C 316, 27.11.1995.

14 For instance, 98/733/JHA of the 21.12.1998; 96/443/JHA of the 5.11.96 and 97/154/JHA of the 24/2/97.

certain specific matters, and states were obliged to abide by such a position in their domestic policies and diplomatic representations. Despite Maastricht being a political breakthrough and the foundation for establishing the AFSJ, the provisions enshrined therein relating to criminal law at the Union level proved to be rather weak.

First, Title VI requires 'cooperation' between States in the field of Justice and Home Affairs, as found in the first and second pillars. Those matters as enshrined within the Title were to be considered as matters of 'common interest'[15] in accordance with the Treaty. In this field, integration was not required. In the third pillar, legally binding action was very limited. Moreover, the structure utilised was rather complicated; working groups and steering groups set up to hasten the legislative process did not last long since Maastricht demanded a unanimous rule for decisions to be taken. The reasons outlined above meant that the performance was rather poor. Due to its failure to achieve its promulgated objectives, the Maastricht 'third pillar' is considered a failure. Beyond the symbolic significance of justice and home affairs on the European table, using Conventions as a vehicle for legally binding instruments did not work well. The objectives within the Justice and Home Affairs pillar were ambiguous, while the European Parliament and the CJEU were excluded, respectively.

5 The Need to Adapt to Emerging Realities and the Amsterdam Treaty

EU expansion was causing growing concern, and all States had prioritised immigration and security. By then, the Schengen Agreement had taken effect and was developed independently of EU rules and structures.[16] Having two parallel legal systems in the EU became a real possibility. On the one hand, there would have been Schengen and third-pillar norms on the other. It was an undesirable situation that created legal uncertainty, so it became an issue requiring corrective action. Members of the Intergovernmental Conference[17] in 1996 leading to the Amsterdam Treaty wanted to achieve solutions to a series of challenges experienced at the time, including *inter alia* issues related to Schengen. At the time, it was believed that the most appropriate means to solve the challenges encountered in this respect was to 'communitaurise' the

15 See Mitsilegas, V., *Modern Studies in European Law: EU Criminal Law*, Hart Publishing, 2009, p. 10.

16 Peers, S., *EU Justice and Home Affairs Law*, 3rd Edition, OUP, 2011, Oxford, p. 140.

17 Brussels, 17 June 1996 (18.06), CONF 3860/1/9.

entire area, integrating Schengen.[18] The rationale behind such a belief was that this would have incorporated Schengen within the framework of the European Community Treaty.

A similar approach would transfer the fields of asylum, immigration, judicial civil law, and visas to the Community, leaving criminal law and police issues to cooperation within an improved intergovernmental framework.[19] Due to the pillar structure in the European Union established by Maastricht, European criminal law had limited scope for development and cross-border application. This led States to discuss and review the pillar structure of the European Union. Developments in this field profoundly impacted EU criminal law and its application in domestic law.

As a result of the Amsterdam Treaty, the third pillar of Maastricht was divided into two. Most issues in the third pillar were assigned to the first one. Matters pertaining to crossing external borders, asylum, judicial cooperation in civil matters, migration policy and status of third-country nationals were 'communitaurised' by being transferred into the first pillar. This transfer meant that within any of the topics transferred, the EU could use 'European Community' procedures and instruments to promote development and bring about change, such as directives and regulations, procedures and developments, which are considered more effective than the traditional third pillar instruments. The transfer also meant that these issues or topics fell under the competence of the CJEU.[20]

The 'communitaurisation' process was far from complete because the third pillar had yet to be eliminated completely; this notwithstanding, the European Union's role had notably been enhanced.[21] Post-Amsterdam, at the decision-making level, the Council still retained the obligation of unanimity within the third pillar.[22] The role of the European Parliament was still modest.

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18 On 'communitaurisation' see also *The Evolution of Supranational Differentiation Assessing Enhanced Cooperation, the Area of Freedom, Security & Justice and the Common Foreign & Security Policy under the Treaties of Nice and Lisbon Priv.-Doz.* Dr. Daniel Thym LL.M. Faculty of Law, Humboldt-University, Berlin, 2009: https://www.rewi.hu-berlin.de/de/lf/oe/whi/publikationen/whi-papers/2009/whi-paper0309.pdf accessed on 20th May 2024.

19 Petite, M., *The Commission's Role in the IGC's Drafting of the Treaty of Amsterdam*, Article 5, in Fordham International Law Journal Volume 22, Issue 6, 1998, p. 83.

20 See also Weyembergh, A., "Building A European Legal Area: What Has Been Achieved And What Has Still To Be Done?", Seminar "*Justice and Home Affairs – How to Implement the Amsterdam Treaty?*", Paris 13 and 14 April, 2000.

21 See also Dashwood, A., "*Issues of Decision-making in the European Union after Nice*", in Arnull, A., and Wincott, D., (eds), *Accountability and Legitimacy in the European Union*, Oxford, OUP, 2002.

22 Article 34 TEU.

Parliament had to be regularly informed of discussions within the third pillar,[23] merely be consulted in adopting binding instruments (such as Decisions, Framework Decisions and Conventions) and make recommendations.[24]

Police and criminal justice cooperation were retained in the reformed third pillar. While the Commission was afforded some right of initiative, this was not exclusive; it was shared with Member States. Member States were also granted a notable right to propose third-pillar instruments.[25] Consequently, despite having limited competence, the CJEU enjoyed a degree of competence *vis-à-vis* legal instruments, which fell within the confines of the reformed third pillar. Amsterdam sought to reform and resolve the aforementioned failures, and indeed, post-Amsterdam, the third pillar was more focused, strengthened the legislative instruments to be used, and permitted limited intervention by the institutions. In this respect, one must appreciate that serious efforts were made to attempt to boost the third pillar to permit further development of criminal law norms.

Furthermore, it must be highlighted that Amsterdam played a pivotal role in altering the type of instruments employed. While common positions were retained, their legal nature was clearly defined.[26] Notably, European Courts have constantly emphasised the obligation imposed upon Member States to abide by common positions while simultaneously affirming that each Member State was obliged to satisfy their pertinent obligations as enshrined under Union law.[27] The Joint Actions, which had posed several issues, were abolished. In their stead, two binding instruments served as their replacement, namely framework decisions for approximation of laws[28] and decisions for any other purposes.[29] Within the reformed third pillar, while Conventions are still permitted[30] to be rendered binding on all Member States respectively, they now merely require the adoption by half of the Member States. Therefore, the cumbersome challenge posed by the consensus requirement was overcome.

Undoubtedly, Amsterdam positively impacted the development of EU criminal law and formed a novel foundation for subsequent reforms. Estella Baker affirms that post-Amsterdam, the third pillar became a 'strange creature'

23 Article 39(1) TEU.
24 Article 39(2) and (3).
25 Article 34(2) TEU.
26 Article 34(2)(a) TEU.
27 See Case C-354/04 *P, Gestoras Pro Aministia et al v Council*, ECR [2007], I-5179 and Case C-355/04 P, *Segi et al v Council,* ECT [2007] I-6157, para.52.
28 Article 34(2)(b) TEU.
29 Article 34(2)(c) TEU.
30 Article 34(23)(d) TEU.

because whilst it had a hint of supranationality, simultaneously, it remained entrenched in a truly intergovernmental structure.[31] Hence, serious shortcomings within this pillar lingered, notwithstanding the various efforts at corrective action.

6 Further Evolution via the Treaty of Nice

The third pillar of the European Union was further corrected by virtue of The Treaty of Nice, more specifically, Article 40 enshrined therein.[32] This article provides that such cooperation ought to have, as its purpose, the goal of allowing rapid development within the European Union for the latter to become an area of freedom, justice and security, respectively. Another notable development brought about by the Treaty of Nice pertains to the fact that it widened the scope of the CJEU's powers in this area.[33] Nonetheless, despite the progress outlined above, this Treaty of Nice had numerous rather serious shortcomings. The primary shortcoming is evident in the fact that it did not abolish the pillar structure. Another shortcoming relates to the fact that various pressing matters were left unaddressed. The third shortcoming is that the Treaty did not successfully implement a rather significant proposal for establishing an EPPO. Last but not least, the Treaty did not succeed in adopting a binding Charter of Fundamental Human Rights despite a proposal to this effect being set forth by the Commission.

7 *Pupino* and the Lisbon Treaty

These shortcomings and others imperatively called for an improved solution to be agreed upon by Member States. Notwithstanding this, the pillar structure began to erode. The central legal instrument in the third pillar refers to framework decisions[34] because while they are binding as to the results to be achieved, they allow Member States a degree of freedom in determining which legal instruments are necessitated to achieve the desired result on a domestic

31 Baker, E., & Harding, C., *From Past Imperfect to Future Perfect? A longitudinal study of the third pillar, European Law Review, Sweet & Maxwell,* E.L. Rev. 2009, 34(1), 25–54.

32 The Treaty of Nice was signed by European leaders on 26 February 2001 and came into force on 1 February 2003, OJ 2001/C 80/01.

33 *Vide* Article 40, TEU.

34 See also Borges, J.M., *Implementing Framework Decisions*, *Framework Common Market Law Review* 44: 1361–1386, 2007. Kluwer Law International, 1361, 2007.

level.[35] Framework decisions are not designed to require direct effect.[36] However, in appreciating this position, one must consider the *Pupino* case.[37]

The *Pupino* case involved a kindergarten teacher in Italy (Maria Pupina) who was accused of mistreating children under her care. The Italian court referred to the European Court of Justice the question of whether national law should be interpreted in light of a Council Framework decision made under Pillar Three or whether the 'duty of harmonious interpretation' under Pillar One also applied when interpreting national law; on its part, the ECJ confirmed that this interpretive duty also applied to Pillar Three decisions. With framework decisions binding on Member States regarding results to be achieved, these place an obligation on national courts to interpret national laws in conformity with this goal. The fact that the ECJ has a lesser role under the third pillar does not detract from this point, and the drafters of the Amsterdam Treaty intended legal instruments with effects similar to those under Pillar One to contribute effectively towards the Union's objectives. This case again set the constitutional ball rolling because it extended supranational principles in a rather controversial manner, namely the notions of effectiveness and loyalty emanating from Article 10 EC. This landmark judgement truly shed light on the possibility of establishing a federalist supranational legal order.

Despite not being an absolute principle, the principle of direct effect may entail an individual's right to invoke and rely on provisions of European Union law before the domestic courts.[38] This also holds true in cases where the provision of European Union law was not implemented at all or where it was implemented incorrectly.[39] This principle of direct effect will be wholly operational once the transitory period set out in the Lisbon Treaty expires, when all Framework Decisions should take direct effect in all Member States, notwithstanding the fact that some Member States had entered reservations to this notion before Lisbon. It must be affirmed that Framework Decisions enjoy immediate direct effect after Lisbon. In the aftermath of the the *Pupino* case, domestic courts are now bound with an interpretative obligation giving *indirect effect* to provisions of Union law. The latter was achieved by imposing an obligation upon domestic courts to interpret national law that conforms with, and runs parallel to European Union law. It must be affirmed that this type of obligation

35 Article. 34(2)(b) TEU.

36 Framework decisions are not designed to be used for harmonization of law but rather approximation. For more see Ch. 2.

37 Case C-105/03, Maria Pupino, ECR [2005], I-5285.

38 As was established in Case 26/62 *Van Gend en Loos* (1963) ECR 13.

39 Given also the principle of supremacy of EU Treaty law as was established In Case 106/77 *Administrazione delle Finanze v Simmenthal* [1978] ECR 629.

remains confined by general principles of law, including *inter alia* the notions of legal certainty and non-retroactivity, respectively.[40]

Moreover, this obligation may not be employed to achieve an interpretation that would violate statutory domestic norms (*contra legem*). However, it ought to be used to ensure that national legislation is, as much as possible, interpreted in a way that gives full effect to provisions of European Union law. Post-Lisbon, this principle is still applicable *vis-à-vis* Framework Decisions and other instruments.[41]

The landmark *Pupino* judgement opened a pandora's box, questioning whether third-pillar measures can be considered supreme. Indeed, it raises the issue of whether domestic law may be set aside if a conflict with third-pillar measures arises. In this respect, the Courts of Justice of Europe provide no *dictum*, but various arguments point in this direction. According to Judge Koen Lenearts, this was the norm.[42]

Therefore, it is suggested that for the goals of the Treaty to be achieved successfully, third-pillar measures should be applied and respected. Third-pillar measures must be strictly respected and upheld, meaning that a situation whereby domestic law runs counter to third-pillar measures would not be deemed acceptable. Nonetheless, it must be affirmed that limitations to such a principle exist, such as the fact that Treaty law may not be used *contra legem* against national law.

Respect for fundamental human rights remained a primary concern for Member States, especially due to the fact that the third pillar may be said to be intergovernmental in nature. Indeed, such a concern brought about a rather worrying sense of mistrust among Member States, as the latter were doubtful about the overall degree of respect that human rights enjoyed across all the different Member States. Against the backdrop, in 2004, the Commission advocated for the Framework Decision on Procedural Rights in Criminal Proceedings.[43] Renewed vigour was given in 2006[44] when incorporating

40 Case C-403/02 *Berlusconi* (2005) ECR I-3656 established that a person cannot be convicted or punished solely on the basis of a Framework Decision and in the absence of an implementing domestic law or other domestic norm.

41 Blackstone's Criminal Practice 2012, Oxford University Press, 2012, para A9.5.

42 Lenearts K., and Corthaut, T., *Of Birds and Hedges: the Role of Primacy in Invoking Norms of EU Law* (2006) 31 European Law Review 287, pp. 289–290.

43 Commission's proposal for a Council Framework Decision on certain procedural rights in criminal proceedings throughout the European Union, COM(2004) 328 final.

44 Communication from the Commission to the Council and the European Parliament 'Implementing the Hague Programme: the way forward' of 28 June 2006, COM (2006) 331 final.

Procedural and Defence rights in the Hague Programme[45] and, more recently, in the Stockholm Programme.[46] The adoption of human rights within the third pillar meant that it was notionally easier to apply and enforce third pillar measures on national legislation.[47] Indeed, the self-contained third pillar continued to erode significantly by virtue of the decision in *Pupino* alongside other developments that occurred in the interim. Eventually, the discussion arose about whether it was possible to abolish the third pillar completely and 'communitaurise' the same one, bringing it in line with the first one.

It must be noted that various amendments that came into force due to the Lisbon Treaty have had a rather impactful impact on the AFSJ. Article 83 paragraph (1) TFEU replaced the former Article 31 paragraph 1 letter (e) TEU. Notably, the change in this regard has been rather significant. A significant alteration occurred when Lisbon completely abolished the pillar structure, whereby all the pillars were, so to say, 'absorbed' within the first pillar structure. Hence, this meant that justice, security and freedom did not remain solely within the remit of Member States, while the European Commission enjoyed a monopoly over the right of initiative.[48]

Moreover, the European Council no longer decides by virtue of unanimity but by a qualified majority voting. Meanwhile, the European Parliament is involved in the procedure and possesses the power to bring a proposal to an end. The Court of Justice also plays an important role in ensuring that Community law is interpreted uniformly.

Therefore, it is evident that Lisbon brought about a significant shift in competencies. The power of national governments was somewhat limited, while simultaneously, there was an extension of the powers of the European Parliament. Indeed, this development was positively regarded as increasing the democratic aspect within the European Union. Moreover, this shift also brought about a change in the form of the legal instruments involved, as directives replaced framework decisions. This reform greatly impacted the operation of the AFSJ.

45 COM(2005) 184 final, O.J. C 236 of 24.9.2005.

46 O.J. C 115 of 4.5.2010.

47 See also De Cecco, F., *Room to Move? Minimum Harmonization and Fundamental Rights,* Common Market Law Review: 43, 9–30, Kluwer Law International, 2006.

48 See also Herlin-Karnell, E., *Effectiveness and Consitutional Limits in European Criminal law*, NJECL 2014/3, Intersentia, 2014.

8 Organised Crime and Europol

The historical and legal development of the AFSJ sheds light on the reasons behind the lack of standardization of criminal norms within the AFSJ and why Member States have been charged with the effective implementation of Directives within their domestic sphere. Consequently, the compromise is achieved at the level of national implementation. It also highlights why certain mutual recognition instruments have been pushed forward, why the Commission has promoted certain agencies such as Eurojust, Europol, and OLAF, and why uniform implementation and enforcement procedural safeguards remained weak and lacking.

In parallel to legislating EU norms within a 'territory', States also formed a keen interest in further enhancing and developing cross-border monitoring and investigative tools, enabling them to discover criminal activity and coordinate investigations to collect data and evidence within the Member States' territories. These legal developments are important as they enhance the relevance and effectiveness of implementing EU penal norms. This signified further specific implantation in national law. Moreover, it was evident that in matters related to organised crime, where a political will was undoubtedly the strongest, the greatest development was registered in the proliferation of new qualitative EU penal norms. Efforts to curb organised crime have generally brought about political consensus. Consequently, the traditional resistance to developing novel criminal rules at the European Union level did not pose a problem. In brief, in those instances where states demonstrate a shared willingness, few legal obstacles that cannot be overcome in criminal law at the European Union level present themselves, rendering the idea that a federalist EU criminal law structure is truly plausible.

The so-termed Trevi Group was of great significance in developing the AFSJ. This Group[49] was originally established to fight terrorism.[50] Trevi 3[51] was assigned the task of dealing with serious organised international crime and drug trafficking, respectively. This working group greatly assisted in gathering momentum for inter-state cooperation to fight transboundary crime impacting European nations. The discussions proved to be successful and led to a positive outcome. Interstate cooperation was the solution to fight transboundary crime in an organised manner. This first working group was limited to dealing

49 The Trevi group was set up in 1976.

50 Practical Police Cooperation in the European Community, Home Affairs Select Committee, HC 363-I, 1 (UK), 8.4.90, p6.

51 Trevi Workgroup 3 started functioning in 1985.

with drug trafficking. Trevi 3 further enhanced such cooperation by encompassing other areas of criminal activities, including *inter alia* armed robbery, the issue pertaining to organised vehicle theft, the protection of witnesses, non-cash payments which were illegal in nature and the protection of cultural property. The group also aimed to promote cooperation in training courses to combat violent organised crime. At the same time, the same group also worked towards addressing the issue of border immigration controls until, eventually, in 1989, the Trevi 92[52] working group took over.[53]

Trevi did establish a common ground. An important agreement was reached *vis-à-vis* the key offence of 'terrorism', which was defined as: "the use and attempt to use violence by a structured group to obtain political objectives". It should be noted that defining this term has been no easy feat. Another term agreed upon is 'organised crime', defined as 'an uninterrupted series of criminal activities committed by a group of individuals to obtain benefits, influence or power'.[54] The consensus reached over such terms also represented a sizeable leap towards establishing common substantive norms and rules for such offences. Trevi demonstrated that where there was political will, it was possible to establish uniform, harmonised or at least agreed criminal law offence definitions applicable across the Member States of the European Union.

Nonetheless, Trevi suffered from a major drawback because it did not enjoy a formal legal structure or standing under European Union Law. Despite somewhat lacking in this respect, Trevi brought about four important documents which were published in its wake, namely:

i. the 'Palma Document';[55]
ii. the 'Declaration of Trevi Group Ministers';[56]
iii. the 'Programme of Action';[57] and
iv. the Coordinators' report on the progress of the Palma Document (Edinburgh, December 1992).[58]

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52 During the meeting of Trevi Ministers in London on 1 December 1992, minutes of the meeting on 16–17 November 1992, Trevi Secretariat, Home Office, UK, reveal that it was agreed that Working Group III would take over the work of Trevi 92.

53 Bunyon., T., *Trevi, Europol and the European State,* in Statewatching the New Europe, 1993, p. 3.

54 *Ibid.*

55 Agreed to in Madrid, June 1989. See also Bowling, B., and Sheptycki, J., *Global Policing*, Sage, London, 2012, p. 43.

56 Agreed to in Paris, 15 December 1989. See also Bevir, M., Daddow, O., Hall, I., (eds.), *Interpreting Global Security,* Routledge, 2013, p. 151.

57 Agreed to in Dublin, June 1990.

58 Agreed to in Edinburgh, December 1992.

These documents are noteworthy when seeking to appreciate the AFSJ. The 'Palma Document' reviewed the objectives of Trevi and was endorsed during the 1989 EC Council meeting held in Madrid, Spain. This revision and the Programme of Action[59] led to establishment of the European Information System (EIS) and the European Drugs Intelligence Unit. The report was also pivotal in creating Europol. Therefore, these Documents were of seismic significance to the development of the policing aspects of the AFSJ. The 1989 Declaration of Trevi Ministers created a further motivation towards developing coordinated responses to organised crime while simultaneously manifesting the political desire to address and combat serious organised crime effectively. It called upon States to establish a "European area without internal borders" and effective cooperation geared towards "fighting terrorism, international crime, narcotics and illegal trafficking of every sort". This declaration was essential to provide the political impetus for creating an AFSJ within a European context. This was not the end but rather the beginning as considerable work was being undertaken. The European Commission and the Council of Ministers published a document on how the AFSJ60 could be further developed.

It was undoubtedly necessary to achieve common principles geared towards effective negotiation and drafting of norms to permit States to embrace similar criminal notions and definitions throughout the various dissimilar criminal law systems present. Indeed, Jurists believed that any self-respecting European-wide criminal law system required common principles to pave the way for further development. Hence, it is unsurprising that an arrangement was reached after extensive negotiations, and common principles were notably agreed upon. Such principles allowed for the application of common rules whilst simultaneously providing the necessary legal flexibility for effective application across the various dissimilar criminal law systems. The significance of these principles cannot be understated. Essentially, such principles made it possible for future developments in the field of criminal law at the European Union level, both from a quantitative and qualitative perspective.

59 Agreed to by the Council of Ministers in Trevi, Dublin, June 1990.

60 Commission of the European Communities, *Towards an Area of Freedom, Security and Justice*, MEM0198155, Brussels, July 15, 1998; Council of Ministers, *Action Plan of the Council and the Commission on How Best to Implement the Provisions of the Treaty of Amsterdam establishing an Area of Freedom, Security and Justice*, 13844198, Brussels, December 4, 1998.

9 The Principle of Mutual Recognition and Assistance in the AFSJ

The creation of the AFSJ shed light on the vast legal differences that characterised the criminal law systems adopted by Member States. It was evident that establishing common principles was essential in attaining mutual assistance and cooperation. It was also evident that political compromise dictated flexibility in European instruments to permit Member States to implement such criminal rules within their respective national legal structures. Mutual recognition reiterates the legal diversity of Member States whilst simultaneously urging Member States to accept as valid certain requests and decisions by other Member States.[61] This is a step in the right direction, which, nonetheless, requires a certain level of compromise at the expense of unambiguous and transparent procedures and, more importantly, at the expense of the protection of procedural safeguards for arrested individuals. It is only by virtue of such principles that EU norms could, in practice, be applied in the respective domestic legislation of Member States, as opposed to a harmonisation process.

All cooperation between States was rendered intergovernmental by virtue of the 1992 Maastricht Treaty, which ought to be differentiated from the Community Structures. In summary, any negotiations, discussions, and cooperation efforts employed and achieved were interstate, not union-promoted or based. It was understood that for true progress to be achieved, the establishment of a more unifying set-up was paramount. Indeed, a balance was struck by virtue of the Maastricht Treaty between, on the one hand, the establishment of an improved and novel cooperation mechanism within the Unions' new structures and, simultaneously, the retention of its intergovernmental nature. This was achieved through a new distinct pillar, the Justice and Home Affairs pillar.

The 1997 Amsterdam Treaty positively impacted *vis-à-vis* cooperation within the crime enforcement field, marking a new age in this respect. Indeed, efforts turned towards the central objective of establishing an AFSJ.

It is important to note that the Amsterdam Treaty also integrated traditional intergovernmental issues such as visas, asylum, immigration and free movement into the Community framework. At the time when the Amsterdam Treaty was coming into force, the European Council organised an *ad hoc* meeting, which took place in Tampere in 1999. The meeting was geared towards discussing the establishment of an AFSJ within the European Union. The conclusions

61 Merlin, J.B., and Albert, J., *Is the EU Ready for Automatic Mutual Recognition … in the Fight Against Crime?*, EUCRIM 2015/2, Max-Plank Institute, pp. 60–63.

reached by virtue of the said meeting constituted a notable advancement in the overall shaping of criminal law at the Union level.[62]

A series of significant themes shaped the meeting's agenda, which *inter alia* included the establishment of a European Judicial Area, immigration and asylum policy, and combatting cross-border crime.[63] Notably, there was a sense of appreciation that a greater degree of unification, assistance, and cooperation among the different legal systems was paramount to expediting and facilitating proceedings in different Member States where prosecutions involved or required the input or assistance of another Member State. Hence, this begged for a more unified procedural approach within the AFSJ.

However, cooperation and judicial effectiveness required something further, leading to discussions concerning the notion of mutual recognition and approximation of laws. It was understood and established that enhanced cooperation among states and the strengthening of judicial safeguards over individual rights would be achieved by virtue of the mutual recognition of judgements together with the approximation of laws.[64] In addition, Member States were encouraged to ratify the 1995 and 1996 EU Conventions concerning extradition. The idea was to do away with formal extradition between Member States and replace it with a simple transfer of persons.[65] Mutual consent prevailed on mutual recognition of pre-trial orders, especially regarding evidence collection and asset seizure. An interesting proposal was set forth that evidence which had been gathered lawfully in one State ought to be automatically admissible in the trial despite the latter taking place in another State.[66] The European Commission and Council were to set forth a programme geared towards implementing mutual recognition by December 2000.

Proposals were set forth by the European Council, which proposed the creation of joint investigative teams,[67] particularly in fighting drug trafficking and human trafficking, respectively.[68] The European Council further proposed

62 See also Janssens, C., *The Principle of Mutual Recognition in EU Law*, OUP, Oxford, 2013, p. 184.

63 Ojala, O., Brax, T., *Presidency Introductory Paper*, Members of the Grand Committee, Parliament of Finland, Special Meeting Of The European Council In Tampere, 1 September, 1999.

64 *Ibid.* para. 33.

65 *Ibid*. para 34.

66 *Ibid.* para 35.

67 See also Rijken, C., and Vermeulen, G., (eds.), *Joint Investigation Teams in the European Union from Theory to Practice,* Cambridge University Press, Cambridge, 2006.

68 Ojala, O., and Brax, T., *Presidency Introductory Paper*, Members of the Grand Committee, Parliament of Finland, Special Meeting of The European Council In Tampere, 1 September, 1999. para 43.

creating a European Police Chiefs operational Task Force to liaise and interact with Europol.[69] It also expressed its desire for greater powers to be afforded to Europol and relative resources. Europol was also perceived as leading in initiating, conducting and coordinating investigations with Member States.[70] Moreover, consensus was reached that to combat serious organised crime effectively, Eurojust should be formed and made up of national prosecutors, magistrates, or police officers from every Member State.[71] Serious economic crimes remained a priority for the European Council, and OLAF was created to serve as a specialised agency in this respect.[72]

Furthermore, numerous other programmes and proposals followed suit. Another crime that required serious attention was money laundering. The latter crime constitutes an essential part of serious and organised crime due to the fact that criminals may ultimately make use of monies or assets attained through illegal means. Hence, this issue had to be tackled for the strategy to be effective. The Council's foremost objective was to ensure that effective measures were introduced to identify, freeze, seize and confiscate proceeds generated through criminal activity.[73] However, it remained unclear how this objective would be achieved throughout the Member States of the European Union. Therefore, how norms at the European Union level could be implemented and the manner of implementation became a foremost concern once again. Moreover, implementing EU norms by applying the approximation of laws principle remains a challenging problem, triggering a new set of legal issues.

Member States appreciated that proper meaningful implementation of any EU penal norm could not be achieved with the prevailing fragmented legal systems still in place. It was well-known that a sense of impunity for transboundary crime, including organised crime, was permitted because of the fragmentation among the various legal systems. Indeed, a legal system allowing for proper investigation, prosecution, collection and transmission of evidence and suspects or sanctioning on a regional basis was lacking despite being of paramount importance.[74] Despite the willingness demonstrated by states to

69 *Ibid*. para 44.

70 *Ibid*. para 45.

71 *Ibid*. para 46.

72 Tupman, W.A., and Tupman, A.J., *Policing in Europe: Uniform in Diversity*, Intellect, 1999, Exeter.

73 Ojala, O., Brax, T., *Presidency Introductory Paper,* Members of the Grand Committee, Parliament of Finland, Special Meeting Of The European Council In Tampere, 1 September, 1999. para 43, para 51.

74 See Calderoni, F., *Organized Crime Legislation in the European Union*, Springer, 2010.

cooperate, this proved to be a challenging aspect in legal terms. Huge discrepancies between legal norms were present due to the fact that dissimilar principles were applicable within the diverse legal systems and, above all, even simple criminal offence definitions varied widely. Indeed, it is no surprise that effective progress could not be achieved unless a degree of basic uniformity or approximation was present between States, or at the very minimum, those States were willing to cooperate.[75] A consensus was reached that there should be an approximation of substantive and procedural rules of criminal law relating to money laundering. Furthermore, it was believed that the predicate offences underlying money laundering should be uniform and sufficiently broad to be applicable across all Member States.[76]

Tampere provided fertile ground for criminal law at the Union level to develop,[77] and undeniably, it went a long way in seeking to establish common substantive and procedural criminal law rules, a detailed Union-based action plan, and an effective Union-wide investigative mechanism. The approach was rational, as consensus was reached that having a common and shared front was of paramount importance, necessitating the approximation of domestic legislation, cooperation and assistance in investigations or executions of freezing and confiscation orders, and the mutual recognition of judgements. Nonetheless, Tampere's greatest achievement was no other than the formulation of principles geared towards facilitating norm creation and application for a multitude of other offences. It provided a foundation from which novel criminal offences could be promulgated within the AFSJ. The notion of mutual recognition is essential to promote judicial cooperation and enforcement. The notion of mutual legal assistance assists in judicial and executive control. The approximation of laws is essential for norm creation, and it does away with the more rigorous and inflexible harmonisation of laws. Such notions facilitate and promote the proper formation of norms applicable across the area. Indeed, in developing such norms, it is clear that particular crimes, including *inter alia* drug trafficking, human trafficking and arms trafficking, were all characterised as constituting serious offences which must be addressed by means of a unified 'union' approach within the Area, instead of a singular and individual approach by the Member States.

75 See also see Vernimmen-Van Tiggelen, G., Surano, L., and Weyembergh, A., (eds.) *The future of mutual recognition in criminal matters in the European Union*, Editions de l'Université Libre de Bruxelles, 2009, Brussels.

76 *Presidency Introductory Paper* by Ms. Outi Ojala and Ms. Tuija Brax, Members of the Grand Committee, Parliament of Finland, Special Meeting Of The European Council In Tampere, 1 September, 1999. para 43, para 55.

77 See Peers, S., EU *Justice and Home Affairs*, OUP, 2006, Oxford. Ch 2.

A roadmap of predetermined objectives identifying *inter alia*, police cooperation, combating terrorism and strengthening the AFSJ within The Hague Programme[78] saw the light of day. Notably, an enhanced degree of cooperation was encouraged amongst Member States, Eurojust and Europol, respectively. The section 'Strengthening Justice' specifically addressed judicial cooperation in both criminal and civil issues. Furthermore, it dealt with mutual trust and the enhanced role which was to be afforded to the European Court of Justice. In addition, the notion of mutual recognition was deemed to constitute a fundamental principle in the development of judicial cooperation in criminal matters. In relation to criminal legal matters, an agreement has seemingly been reached that penal legislation ought to be approximated.

Moreover, it was felt that minimum legal procedural standards must be established. Both elements play a crucial role in identifying and building mutual and shared confidence among Member States. Indeed, it is by virtue of the application of core principles, including *inter alia* mutual recognition and assistance and encouraging mutual assistance and cooperation, that European criminal law may truly develop meaningfully.

10 Concluding Observations

At the EU level, there exists a tension between the desire for supranational, federalist-style agencies or norms and the insistence by Member States on retaining their national competence and sovereignty. This paradox has shaped the evolution of EU criminal law. The European Commission, recognizing the need for effective criminal justice cooperation, initiated enhanced specialised investigative and prosecutorial procedures. However, this proactive stance clashed with the slower progress in safeguarding defence rights and procedural guarantees within the Area of Freedom, Security, and Justice (AFSJ).

Criminal law remains firmly entrenched as a matter of national competence. Each Member State seeks to maintain control over prosecuting its nationals and crimes committed within its borders. The concept of supranational agencies or norms often faces resistance, reflecting the deep-rooted belief in national sovereignty.

78 Communication from the Commission to the Council and the European Parliament of 10 May 2005 – The Hague Programme: ten priorities for the next five years. The Partnership for European renewal in the field of Freedom, Security and Justice, COM(2005) 184 final, O.J. C 236 of 24.9.2005.

Despite these challenges, the AFSJ has undeniably brought positive developments to local legal systems. The increased extent and scope of criminal investigations necessitated practical cooperation. European agencies now play an enhanced role and are better equipped to address transnational crime.

In conclusion, the delicate balance between supranational aspirations and national sovereignty continues to shape EU criminal norms. The journey toward an identifiable EU criminal territory remains both complex and essential.[79]

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Index

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