MAIN FEATURES OF THE HARMONIZED EUROPEAN DESIGN LAW

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Abstract: Product design has basic importance in highly competitive markets. Well designed, aesthetic products are favoured by buyers. Thus design is considered a marketing tool most radically in the USA. It is obvious that companies and authors are interested in effective legal protection against illegal imitation. The International Chamber of Commerce (ICC) estimates that imitations and counterfeit products account for roughly 5-8 per cent of world trade and the direct and indirect damage could be as much as 60-100 billion US dollars per year. A sad consequence is also the 70,000 jobs that are lost each year.1 By the end of the 19th century countries recognized that design protection on a national level is incapable of stopping illegal activity. For this reason international agreements such as the Paris Convention in 1909 were signed. The need for harmonizing design law in Europe appeared in the 60’s. The European Court also faced the problem of market distortion caused by intellectual privilege in its practice. The European institutions issued the Design Directive in 1998 (98/71/EC) to harmonize the most substantial elements of national design laws throughout Europe after long theoretical debates. The task is current as the Commission may carry out an analysis within 3 years of the implementation deadline (28.10.2001.) and that expires this year. The Commission has already issued a proposal for an amendment on the Directive in September 2004 concerning spare parts.

I aim to give an outline of the main characteristics of the harmonization directive in my essay focusing on the definitions compared with the notions of former national design laws. I will also refer to the questions of copyright protection for designs since the relationship between the two forms of protection is regulated by the directive. However I will not examine in this article the Community Design Law (Regulation No 6/2002) what is based on the notions of the Directive but contains detailed ruling on the transfer of rights, procedure etc.

1. Protected subject matter

The most important part of any design law is the definition of the product or article that is protectible. Distinction can be made on the basis of the significant elements of the different notions. Some definitions require industrial applicability, no handicraft item can be subject of protection, or only visually recognizable features are accepted. The former Registered Design Act of the UK from 1949 is a good example of the old fashioned industrial-ornamental design law philosophy. Only visible features were under protection, which were also industrially applicable. The Directive follows the new trend by giving a very broad definition:

According to the EU Directive Art. 1. a) design is: “...the appearance of the whole or a part of a product resulting from the features of, in particular the lines, contours, colours, shape, texture and/or

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materials of the product itself and/or its ornamentation.” A product is defined as any industrial or handicraft item, including parts, packaging, get-up, graphic symbols but excludes computer programs (computer graphics and icons aren’t expressly excluded). No shape is registrable if its form dictated solely by technical functions.

The former German design law (Geschmackmustergesetz) used a very similar definition to the one cited above. A design is a two or three dimensional material form or structure. Features of a product which may be protected include its form, style, structure etc. The feature must be recognizable by human sense (including tactile sense).

The French intellectual property code (1992) Vol. 5. contains the rules of design protection. Protectible was any new three dimensional shape. Wide range definition is used by the French code. Industrial applicability is not a need but any shape dictated by its function and patentible designs are excluded.

The broad definition of the design directive only applies to a non taxative list of the protected subject matter which making it very flexible. Industrial applicability is not a need, also handicraft items are covered. Reproductability is not required though without technical ability to some kind of mass production may considered an article of fine arts which is protectible by other forms of legal protection (mainly by copyright). The lack of industrial applicability requirement is also a characteristic of the widely respected design definition of the ICSID: The industrial design is such a creative activity which aims to define the design quality of the industrially produced goods. These formal qualities are not only external features but basically structural and functional connections that create a coherent integrated system from the view of both designers and users.

The WIPO Model Design Law /section 2(1)/ from 1971 also contained a quite wide scale definition on design: “any composition of lines or colours or any three-dimensional form,... provided that such composition or form gives a special appearance to a product of industry or handicraft or can serve as a pattern for (such) a product.” The protected subject matter pursuant to this definition is the individual appearance of the product, so that only an eye-appeal test is required. Design is defined as an aesthetic creation. A technically functional element is protectible if it also has some aesthetic character and the same technical result could be reached by another shape.

As mentioned above the exclusion for any shape dictated by its (technical or other) functionality used to be a characteristic of all national laws already before harmonization. Sometimes it is hard for the courts to decide whether a feature is technically determined. Four methods of examination is are used in the legal practice of courts on the functionality problem:

1. Multiplicité des formes test (France and Belgium) examines if the designer could have chosen another form.
2. Examination of the presumed intention of the designer (UK).
3. Examination whether alternative design would have been possible with the same function.
4. Examination of the presumed intention of buyers: why their decision to buy the article were made.

Pursuant to the Directive Art. 7. (2) an exception for mechanical connections is given. “A design right shall not subsist in features of appearance of a product which must necessarily be reproduced in their exact form and dimensions in order to permit the product in which the design is incorporated or to which is applied to be mechanically connected to or placed in, around or against another

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product so that either product may perform its function.” It is kind of exclusion that was unknown in the continental regimes was borrowed from the UK’s Act of 1988. (Art. 213 (3) b) i.) In the English law terminology this exclusion is called the exclusion for “must fit features” that are clearly distinct from “must match features”. The so called must match features are excluded effectively by the repair (or spare part) clause (Art 14. and 18.) of the Directive. The most debated part of the Directive is the so called “repair clause” exclusion for spare parts. A spare part is a component of a complex product (protectable under the Directive) the purpose of which is to repair the original appearance of the product “so as to restore its original appearance”. The necessity to restrict the legal protection of such parts is originated from the fundamental idea of the EU to liberalise the movement of goods in the internal market. In the practice of the European Court of Justice it was ruled that the exercise of an exclusive right (design right) may be prohibited by the EC Treaty Art. 86. (Volvo and Renault cases) The Art. 14. is called a “freeze plus formula” which stipulated that Member States may maintain existing laws, any change permitted only in the way of liberalisation of the spare part market. The European Policy Evaluation Consortium analyzed this issue for the DG Internal Market. The EPEC set out four alternatives for future legislation: 1. Liberalization. No design protection of spare parts (at all). 2. A system seeking a short term of design protection, the usual term of protection could be reduced to 10 years. 3. A remuneration system for the use of protected designs, including the appropriate level for remuneration. The independent spare part producers may pay a reasonable remuneration to the right holder. 4. Combination of the above mentioned systems. The Commission carried out an analysis according to Art. 18. In most European countries remained design protection for spare parts. The Commission found that the prices of spare parts are lower where they are not design-protected. According to the proposal of amendment of the directive spare parts would be excluded from design protection. However for consumer protection purposes the MS-s shall ensure information is given to the buyers of the origin of spares. Experts expect enhancement of spare part market after liberalisation.

2. Conditions of registration:

Every local system required that a registrable design be novel and also required some originality. Distinction can be made between objective, subjective, absolute and relative novelty. From the view of a creator, a design is new if it is not an imitation of existing forms known to him is called subjective novelty. It corresponds to a large extent, if not completely, to originality in copyright law, that is that the creator is protected even if the same creation had already been made by another person, unless creator was aware of the first creation. Some call this “copyright approach” because of the theoretical and effective similarities.

From the view of the public, novelty is objective if no identical design was made available to the public without limitations. This corresponds with a generally accepted definition of novelty in patent law, and one speaks therefore of a “patent approach.” However both approaches can have a number of variations: the search for previous products may be limited to the country where protection was required or worldwide. Such a creation may be limited by time, it may be also be limited in regard to manner in which a previous creation was made available to the public, these forms are called relative novelty. Everything which was available to the public no matter where, when and how is excluded from the protection and refers not only previously registered designs but

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includes all existing forms is named by experts as objective-absolute novelty. This kind of absolute novelty requirement was in force in most Mediterranean and former communist countries and it was dictated by the above mentioned WIPO Model Design Law.

Subjective-relative novelty or local novelty was required by the German and Benelux design law. These countries applied an examination system from the view of the relevant local trade circles. A very similar subjective-relative criteria is used by the Design Directive. Art. 6. of the Directive makes clear that public availability means the knowledge of the specialised circles within the territory of the community. It is my opinion that today in the age of the internet, when every part of the world is connected, this kind of local knowledge is questionable. Moreover the specialized circle of designers is relatively small and designers keep close contact with each other in international organizations like ICSID. Under the Directive not only novelty but also individual character is required. This requirement is the copyright approach element of the law. This regime is similar to the former German and French law. Both German and French laws required originality that originates from copyright law. This kind of originality is different from the individual character requirement since it means only that any good must be a personal intellectual creation. According to the originality requirement a shape which is formed without human creativity is unprotectable. An example (of the practice of the Hungarian Supreme Court) can be the case of a tile pattern of which was formed by the production machine automatically due to technological reasons. The individual character in accordance with the Directive means some kind of distinctiveness. The Green Book on design harmonization in its original form suggested the use of the notion distinctive character in the new law instead of individual character because it would have been more straightforward.

The double criterion of novelty and individuality was criticized by some authors because of its controversial with international agreements and logical reason.\textsuperscript{10} The TRIPS agreement Art. 25. requires only one criterion: novelty or individual characteristic/ originality is applicable. It seems that the definition of individual character is interpretable as the mere definition of novelty. Sometimes it is hardly imaginable that a feature which has individual character (in the meaning of the Directive) is not novel. However the two level examination does not cause problems in practice. The courts use a four level test to decide upon individuality:\textsuperscript{11}

1. The judge examine the shape from the aspect of the relevant (it depends on the kind of product) circle of end users.
2. The judge estimates the probable level of the user’s knowledge.
3. Judge examines the cognizability level within the relevant territory.
4. The new design is compared with the formerly known shapes.

3. Duration of protection

The period of protection was ensured by national laws differed on a wide scale before harmonisation. At the lower end was Hungary where maximum duration was only 10 years while at the higher end, in France, 50 years of protection was awarded. The latest modification of the Hague Agreement declared 15 years as a minimum. The unified duration now in the EU countries according to the Directive is 25 years. There is still no accordance between the experts on the ideal length of protection. The optimal term depends mostly on the type of product. It’s obvious that a textile industry article does not need as long a protection as furniture. Problems occur on the market when the right owner take an unfair advantage of the long duration of exclusivity.

\textsuperscript{11}Suthersanen 39-40.p.
4. Design-copyright interface

Copyright is an equally important form of protection like specific design law. According to the opinion of some experts in some fields of production (e.g. textile industry) 99 per cent of designs which in practice have not been deposited are protected by copyright. The advantages of copyright compared with registered design law are as follows: automatic and quick, runs form the creation without any formalities, broad scope protection (design protection is often restricted to a single product) copyright covers adaptations. Copyright provides a long term protection-70 years post mortem auctoris, no novelty is required, and is available free of charge. The only unquestionable disadvantage of this form of protection the difficulty of proof of priority (time of creation). A unique solution exists for the latter problem in Hungary: the quasi registrability of artistic works. A board „jury” recognised by the state examines the goods and registra te them if the requirements are fullfilled. The cost of examination is approximately half of the design registration fee. This “quasi registration” often helps the authors to prove their priority before the courts.

The design directive sets the principle of total cumulation (or overlap) of design protection with national copyright. (Art. 17.) It means that a design may be eligible for copyright protection and so the shape is protectable on both grounds simultaneously. Three slightly different systems emerged prior the Directive and two of them have remained different. Total cumulation: in France and Benelux countries (and e.g. in Hungary). This system is based on the „unité de l’art” theory which means that fine arts and applied arts is indistinguishable. Partially cumulative protection exists in Germany where a higher level of originality and some artistic merit is required. Non-cumulative system was in force in Italy until the implementation of the Directive. Italy excluded designs from copyright protection since separability of artistic value and industrial character was required. The non harmonised originality threshold and other differences between Member States cause inequalities in the EU and distort the single market. The problem occurs in the total cumulative countries where “unité del’ art” principle is followed because it is not unusual to claim copyright protection for spare parts. The spread of this formula in Europe can lead to the deprivation of the liberalisation of spare parts market, the new aim of the harmonized design doctrine.

5. Summary

In my essay I have shown that the notion of design follows from the foregoing national definitions and in many aspects is similar to the ICSID definition of design. A broad scale of articles, also handicraft items, component parts and complex products are protectable under the Design Directive although any shape dictated solely by its technical function is excluded. I mentioned the so called spare part issue at relatively length since the Commission issued its proposal for the amendment of the Directive relating the spare parts this September. The proposal of the Commission would exclude from the protection the component parts which are produced for the purpose of restoring the original appearance of a complex product in order to liberalise the common market.

A two fold system examining the conditions of registrations can be found. Both novelty and individual character is required. The novelty defined in the directive is a co called subjective-relative one.

13 Duration was harmonised by the Duration Directive 93/98/EC which is in accordance with the Berne Convention Article 2.
The principle of cumulation with copyright protection is declared in the harmonized law. I have analyzed in my essay the different forms of cumulation such as non-cumulative, partly cumulative, and total cumulative systems. I have also set out briefly the differences between the specific design law and copyright and both advantages and disadvantages of the latter. The most threatened danger of the non (or partly) harmonized European copyright concerning design protection, is that the spread totally cumulative copyright system can deprive the spare part market of liberalisation.

List of sources:

POST-ACCESSION DUTIES OF LEGAL HARMONISATION

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After the accession Hungary’s duty of harmonisation hasn’t come to an end, since the Hungarian legal system still has the deadlines set by community law to take into account, and our legal system has to give fast and adequate responses to the community’s legal challenges. The State should effectively take part in the decision-making process of the European Union in a way that we could enforce our interests to the most possible extent even after the accession period. It is almost as hard a duty as the accession was and goes with an enormous liability, since after the first of may we will also take part in the European Union’s decision-making process.

In the past decade Hungarian legislation was hardly influenced by the process of legal harmonisation. The aim was to be ready for the accession to the European Union, to fulfil one of the fundamental requirements. Hungary has already made a legal commitment in the European Agreement, signed in 1991 and entered into force 1 February 1994, to approximate its legal provisions to community law. In the pre-accession period the process of harmonisation was hardly affected by the fact that Hungary had to harmonise its laws in a really short period of time to a legal system, which had decades to develop. The great amount and time-consuming character of the duties made necessary the enumeration and programming of the tasks. The beginning of the process was helped by the Commission’s White Paper on the preparation of the associated countries of Central and Eastern Europe for Integration into the Internal Market of the Union.

Besides the fulfilment of the legal obligations and the creation of the legal background the process of preparation for the accession contained supplementary tasks, just like the creation of the institutional system needed for the implementation of the European legal provisions, the training of experts who will take part in the enforcement. This study will only deal with the features characterising the decade of preparation for the accession and with harmonisation duties arising from Hungary’s membership in the European Union.

1. Tools of harmonisation

As regards the amount of duties of preparation, on the day of accession 130,000 pages of legal texts will be in force in the European Union. Hungary has undertaken to be capable of the application of this enormous amount of legal texts. The capability for the enforcement means various means of the preparation and these means are determined by the type of the community legal source.

1. Directives

The directive is one of the main instruments of harmonisation of national laws. Article 94, under the title „Approximation of laws” expressly makes mention to the directive as an act adopted by the Council for the purpose of harmonising the MS’s laws, regulations and administrative acts affecting
the building up and functioning of the internal market. Their characteristic is that they are addressed to the Member States, which are bound to implement them, but remain free in choosing the form and method of implementation. So beneath the so-called minimum harmonisation realized by the directive Member States are free to maintain in force or adopt stricter national rules, since directives do not fix the minimum and maximum level of harmonisation, but only determine the "lowest common multiple".\(^2\)

According to the case-law of the European Court of Justice the adequate tools of implementation are national rules, which are transparent, comply with obligations of the legal certainty and do not leave any doubts in citizens regarding their rights and obligations.\(^3\) In Hungary these instruments can be laws, regulations at a governmental or a ministerial level.

In the event of directives the legal meaning of accession is that for the day of accession it is obligatory to implement all directives, which are in force at the time of the accession and for the implementation of which the deadline is already passed. As a member of the European Union we have to tackle deadlines in a different manner. In the pre-accession period deadlines were determined by the commitments made during the accession negotiations and on the date of accession. After May 2004 the deadlines set by the directives themselves will be boundary. These must be taken into account, since the failure to comply with them means a breach of community law.

In their legal effects framework decisions are similar to directives, and are applied as a legal instrument under the Justice and Home Affairs Pillar. These instruments are also binding as to the end to be achieved and also need to be transposed.

### 2. Regulations

Community regulations are less known by the public than directives, although this type of statutory instruments affects more directly and strongly national legal systems than directives. Community regulations are directly applicable, which means that they are effective from the date of their entry into force without any other act of the national legislator. Moreover it is even forbidden for the national legislator to implement regulations,\(^4\) since it is the only way to ensure that the aim of the legislator, namely the unique application of law throughout the Union can be achieved. Besides all these it is common that community regulations impose on Member States the obligation of enacting enforcement measures. This kind of activity imposes on Member States the duty of legislation, which is not identical with implementation. It can rather be featured as something similar to the activity of enacting implementing decrees in national law for the purpose of implementing national laws. These measures are not to hinder the effective application of the regulations they are rather to serve their appropriate enforcement.\(^5\) In practice quasi-officially two types of regulations are distinkted: basic regulations and implementing regulations.\(^6\) As an example, it is a common practice in connection with agricultural policy that market rules are contained in a Council Regulation, while detailed rules which are necessary for the implementation are contained in a Commission Regulation. The significance of the distinction is that implementing regulations can be annulled without having regard to the issuer.

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\(^1\) Article 249 of the Treaty  
\(^3\) In this respect see C-41/74 Van Duyn v. Home office (EBHT 1985, page 427), and C-143/83 Commission v. Denmark (EBHT 1985, page 427)  
In the period of accession neither regulations nor provisions of the European Agreement were directly applicable. The Council of Constitution has expressed in its decision 30/1998 (VI.25.) in connection with Article 62 paragraph 2 of the European Agreement containing prohibitions in the field of competition law, that Hungarian enforcers can’t apply the criteria of application directly, which refer to and which are a part of community law, contained in this paragraph.  

The prohibition on implementation also means that provisions regulating the same field, which are contrary to regulations or which have a similar content should not be in force in national law. The reason for this is that the relevant territory of legislation is „occupied” by the community legislator, and there is no power left for the Member States to regulate in the area. This is why the appearance of a regulation originates also a duty of deregulation for Member States: national legislator must ensure that national legislation affecting the area is repealed. 

Hungary as an acceeding country also has a duty to give attention to regulations in another respect. In the ten-year period of accession acceding countries have taken into account regulations in the harmonization process during their preparation for the accession. This means that many regulations and provisions of regulations have been transposed similarly to provisions of directives. It hasn’t conflicted with the legal character of community regulations, namely the direct applicability, since regulations are only capable of producing such an effect after the accession. At the same time regulations affecting certain sectors, like agriculture or competition contain fundamental norms, the adaptation to which and the acknowledgement of which could not depend on one date, namely the date of accession because of their economic significance and because of the requirements of legal certainty and abiding by law. The transposition of regulations was accepted and even encouraged by the European Union in the pre-accession period. 

As a consequence of all these the legislator also had to ensure that the harmonised provisions of community regulations should be taken out of the legal system with the date of accession taking into account the effective enforcement of community regulations. The Hungarian legislator had two methods for resolving the problem. On one hand that in the closing dispositions of the implementing legal instruments a provision prescribing that provisions harmonising with the directive will automatically lose force on the date of entry into force of the law announcing the international treaty on Hungary’s accession to the European Union. will be placed. On the other hand in cases when this has not been the case deregulation has to be done before the accession. These tasks were harmonised lately by the ministry of justice within the framework of a submission, which was designed to survey all deregulation tasks affecting the Hungarian legal system and to prescribe harmonisation duties on the right level of legal instruments. 

After the accession deregulation tasks in connection with regulations and legislation duties related to enforcement of laws have to be done fast for the regulation to be capable of being applied without difficulties right from its enter into force. 

Regulations will be available for the citizens and enforcers in the Hungarian language version of the Official Journal of the European Union, which will be a new official source of law in force in Hungary. 

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7 It has to be mentioned that some authors consider this decision to be mistaken and entangled, admitting its direct effect and applicability. See: Imre Vörös: Az EU-csatlakozás alkotmányjogi, jogdogmatikai és jogpolitikai aspektusai, in: Czuczai Jenő: Jogalkotás, jogalkalmazás hazánk EU-csatlakozása későzőben, KJK-Kerszöv Kiadó, Budapest, 2003., 47-49.o.
3. Further legal sources and „negative integration”

Besides directives and regulations, other legal sources like decisions, recommendations and opinions are also liable to produce certain legislation-related duties. Decisions which are boundary for the addressees, are the community law equivalents of administrative acts. Some decisions have a normative character and contain implementing provisions for regulations or directives and that is why they need to be transposed into national law. Recommendations, opinions and other sources of soft law, like communications, guidelines and resolutions are not boundary, but this does not preclude Member States from acting in compliance with them. National courts though have to pay due attention to them when applying or interpreting community law (or national rules related to community law), especially when they contribute to the interpretation of community or national law.8

Recommendations can contribute to harmonisation of laws in another way as well. They can be applied in areas where circumstances are underdeveloped and situation is not yet ready for harder regulation. For example in the area of stock market transactions, a directive enforced the ethical code enacted in 1975 in the form of a recommendation in 1989.9

Another important area of harmonisation is the reflection of the case-law of the European Court of Justice in national law. Fundamental features and characteristics of the enforcement of community law as a legal order free from international and national law were characterised by the European Court of Justice, the only institution to interoperate community law. These are fundamental principles like the supremacy of community law, direct applicability, direct and indirect effect, which have became determining attributes of enforcement and application of community law. National laws must be ready for the application of these principles.

In the above I mentioned those tasks arising from community law, which are to ensure the compliance with secondary acts issued by community institutions. Harmony between national and community law should also be ensured in areas where there are no harmonisation provisions in existence, but there are prohibitions based on primary legislation, on the provisions of the Treaty of Rome. This is what is called by literature negative integration, opposed to what is called positive integration, the feature of which is that it is regulated by harmonised, concrete provisions of regulations and directives. This kind of a duty is for example in the area of free movement of goods the principle of mutual recognition, which prescribes that goods which are legally manufactured and sold legally in a Member State should not be precluded from being sold in the territory of another Member State, save based on grounds of public health and public security.

II. Changes in harmonisation duties after the accession

The amount of duties is obviously different before and after the accession process, since before the accession the implementation of the whole acquis had to be ensured and coordinated. We had to approximate our law to almost 1800 directives, 6000 decisions, to almost 10 000 legal texts of secondary legislation. After 1 May 2004 it will be only the acts enacted later to which we will have to adjust. After the accession besides changes in the amount of duties two fundamental changes are to come. Firstly, legal harmonisation won’t be valued as the preparation for a future event, namely the accession, it will be the mere compliance of a duty coming from Article 10 of the Treaty, the clause of sincere cooperation.

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8 C-322/88 Salvatore Grimaldi versus Fonds des maladies professionnelles (EBHT 1990. page 4407. o.)
As a consequence sanctions of failure to act and institutions based for the enforcement of sanctions and procedures are also different. During the accession period the Commission has evaluated the process of implementation in the acceding countries in its annual reports. The Commission had expressed its critiques and experiences within the framework of these reports, but it could impose no sanctions, it could only postpone the date of accession.

The sanctions for the member states for the failure in the field of approximation of laws are contained in the Treaty. As the last instance the procedure of the Court of First Instance can be initiated, but national courts and the Commission as the guarantor of the Treaty also has an important role to play in creating the harmony between national and community law.

If Hungary as already a member of the European Union fail to implement or implements incorrectly a directive or in another way breaches community law (as an example enacts a national law contrary to community law) it will be made liable for the damages caused to its citizens and others. Liability of the member states for damages is even strengthened by the fact that they can be made liable not only for the failure to fulfil their implementation duties but also for the failures of their administrative authorities –in cases where implementation was done in time and correctly but the authorities of the member state did nothing for the enforcement, and also in cases when supreme courts of the member states infringe community law.

After the accession the directives themselves will determine dates for the implementation and Hungary will have no opportunity to determine the date by itself taking into account political and economical arguments. In the period of the European Agreement, the legislator had used this method frequently, postponing the entry into force of laws, which affected our general interests even till the last date, the date of the entry into force of the Accession Treaty.

The other important hangmen is that Hungary, as a Member state will take part in the Union’s decision-making process. Participation in the technical preparation of legal instruments is especially important, since here participants have equivalent rights in discussing the different alternatives for decision, and in the last phase of the decision-making process small states are in a disadvantage in comparison to greater ones because of their fewer votes.

Taking part in the Union’s decision-making process have two main consequences: partly there is no need for starting the programming of harmonisation by unifying the great amount of legal texts enacted in a long period of time in one program, since duty to approximate will originate from legal instruments of the community issued individually, partly, taking into account that ministries responsible for the enactment of certain kinds of acts are already designated, this designation can be seen as the designation of the ministry responsible for starting the programming process related to the implementation, moreover the starting date of the process is also at our dispose, since it is determined in the date of the end of the decision-making process.

III. Institutions for the performance of duties of harmonisation

As it becomes obvious from the abovementioned, compliance with community law is a multifold activity. It requires the creation of a system, order within the administration that ensures the most effective way the fulfilment of the tasks arising from community law’s provisions. The last decade, the decade preceding the accession can be characterised as a training period, the experiences of which should be used after the accession.

10 See C-6/90 and C-9/90 decision in Francovich case (EBHT 1991. page 5357)
Hungary had chosen the model of centralized coordination, which is successful and that is why should be maintained in the future as well. This coordinating activity of legal harmonisation was the duty of the ministry of justice even from the start, but all ministries had to prepare the plans for harmonisation in their own territory.

After the accession it will be altered by a Government Resolution enacted in April 2004. According to the new regulation, the responsible ministry (or other state-body) will be the one, which was already responsible for the development of our standpoint for the discussions, and which has taken part in the decision-making process of the Union, in the future. As regards the implementation of the already adopted and published EU acts the so-called approximation proposals are to be submitted. The approximation proposal indicates the EU act to which it pertains, specifies the steps necessary in national legislative process and the level of legal instruments required, any legal act that has to be amended, the ministry in charge of the process, and the time limit within which is has to be completed. The deadline must be determined with regard to the deadline for enforcement determined by the community legal instrument. The deadline specified has to indicate the month and year, indicating the date release for administrative debate, and the date of the respective Government decision (or adoption of the ministerial decree), and furthermore, the date proposed for Parliamentary decision.

The Minister of Justice has multiple duties on different levels of legislation, which contain the harmonisation of legal harmonisation duties. Within its framework the Minister works out the order of programming legal approximation duties, arranges tasks in a database, follows with attention and promotes the performance of tasks related to harmonisation and ensures theoretical and technical unity of activities of legal approximation. Firstly it is worth to mention his coordinating activities.

Harmonisation must be performed on the level, which is required by the Legislation Act for the regulation of the same area for the adoption of legal instruments of national law by the Legislation Act. For the preparation of these laws the minister responsible for the topic is responsible. Before the accession it was the task of the Minister of Justice to arrange the great amount of community legal acts in an agenda for the date of accession according to the submissions of the ministries, which was enforced annually by the government in a decree. This was called the program of legal harmonisation, which after the accession should not be performed in such form, but the government’s submission of action plan and legislation program should be created with regard to the submissions on legal approximation. After the accession this will only affect newly enacted

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12 Government Resolution 1036/2004. (IV. 27.)
13 Programming of the legal harmonisation was performed into the following government decrees:
- Gov. Resolution 2174/1995 (VI. 15.) on the five-year program of legal harmonization
- Gov. Resolution 2282/1996 (X. 25.) on the amendment and consolidation of the programs on internal market integration and on legal harmonization preparing the accession to the European Union
- Gov. Resolution 2212/1998 (IX. 30.) on legal harmonisation program for the period till 31. December 2002, and on duties connected to the implementation of the program
- Gov. Resolution 2128/1999. (XI. 5.) on the amendment of government. Regulation 2212/1998 (IX. 30.) on legal harmonisation program for the period till 31. December 2002, and on duties connected to the implementation of the program
- Gov. Resolution 2158/2001 (VI. 27.) on the amendment of government. Regulation 2212/1998 (IX. 30.) on legal harmonisation program for the period till 31. December 2002, and on duties connected to the implementation of the program
- Gov. Resolution 2099/2002 (III. 29.) on the legal harmonisation program and on duties connected to it
- Gov. Resolution 2072/2003 (IV. 9.) on legal harmonisation program and on duties connected to its implementation
- Gov. Resolution 2065/2004 (III. 18.) on legal harmonisation program and on duties connected to its implementation
Post-accession Duties of Legal Harmonisation

Legal acts. The approximation proposals will be integrated into the legislation process. In preparation of the Government’s six-month action plan and legislation program the approximation proposals submitted for the bills tabled for the purpose of approximation must be taken into consideration. With regard to ministerial decrees, the competent ministers take into account of the approved approximation proposal and incorporate them into the ministry’s action plan. Any amendment that may be contained in the action plan and the legislation has to be recorded in the approximation databank, which is created and operated by the Ministry of Justice.

Programming is only reasonable when it is carefully looked after. This process and the acknowledgement of which legal instrument implements which instrument of community law is promoted by the harmonisation clauses placed in the closing dispositions of laws. These must refer concretely to the relevant community instruments and to the level of harmonisation. This clause serves a double aim: on one hand it fulfils the obligation arising from directives that measures taken by Member States must contain reference to the directive. On the other hand it makes possible to search the legal instruments of national law which implements community law. This information is really useful since it is not a requirement of community law that a directive should be implemented by one single act, the task of implementation can also be featured with regard to the national characteristics of national laws in different legal instruments of the same or of a different level. The only requirement is that the legal instruments in whole should cover the whole directive in content. The harmonisation clause promotes to a great extent the following of implementing measures, implemented community law provisions. The form of references is to be determined by the Member States themselves according to the standard form of directives. In the period of the European Agreement the reference to the Agreement was made obligatory by the ministerial decree of the minister of justice 12/1987 (XII.29.), amended by the ministerial decree of the minister of justice 13/1995 (VI.29.). After the accession these references should not be used. The determination of a new legal base is not obligatory, since the obligation to make a reference in case of directives comes from the directives themselves, and in the case of other instruments it is an obligation undertaken by the Member States.

The clause should by its terms cover two groups. The first group contains directives, which need implementation, and normative decisions, the enforcement of which also needs implementation, and sources of soft law, which the legislator want to transpose into national law, while the other contains those regulations for the implementation of which national measures has to be done, national legal acts have to be enacted. The two distinctible groups need the application of texts of different terms.

The practice will be maintained even after the accession that legal harmonisation clauses should be placed among the closing dispositions of legal instruments. It is worth to consider however that the clause should have an own title instead of being placed under the title of closing dispositions. This would facilitate transparent search for the clause as the clause containing information about community law. For the content of the legal harmonisation clauses and for the placement of them in the system of legal norms guidance will be given by the ministerial decree of the minister of justice 12/1987. (XII.29.), amended by ministerial decree of the minister of justice 17/2004 (IV.27.).

Duties of harmonization cannot be performed by the mere acknowledgement of the fact, that a certain instrument of the legal system contains a clause asserting that harmony between national and community law already exists. Only harmony in content and quality can be considered as fulfilment of the duties. Incorrect implementation, national legislation contrary to provisions of community regulations is an infringement of community law. That is why the compatibility has to be examined before the acceptance of statutory instruments, in the period of drafting. Introduction of a bill concerning a law aimed at legal harmonization before the Parliament, and the acceptance of governmental decrees serving the same aim, needs the prior consent of their minister of justice, in case of a ministerial decree only the opinion of the minister of justice is required. This deficiency of
the present system is to be eliminated by the draft of the new legislation act, which requires the consent of the minister even in case of ministerial decrees. In these cases in the event of a debate between the ministry of justice and the relevant ministry, the government would be made responsible for making the decision. This provision would hardly promote the effectiveness of the control over the activities of legal harmonization of the minister of justice.

The storage and refreshment of data about this huge amount of legal instruments and following with attention the activity of legal harmonization nowadays can only be resolved by the modern instruments of informatics. This aim was served by the formation of the database on legal harmonization developed by the ministry of justice, which will be achievable for the public on the Internet after the accession according to the plans of the ministry.

After the accession the minister of justice and the foreign minister will be responsible for the following with attention of the negotiations concerning the draft of the union during the decision-making process, and this way they will be able to control if there is a need of making a submission on legal harmonization and when it should be done.

The fulfilment of legal harmonization duties, the following with attention of the preparation of the drafts will be the task of the minister of justice. Its official form is the report on legal harmonization made every half-year for the government. If in case of certain tasks of harmonisation there is a need of sudden act or there is a significant lag these also have to be submitted to the government individually.

The last station of the harmonisation process is the notification to the European Commission, and the forwarding of the written form of the announced act. This duty originates from Article 10 of the Treaty, which prescribes that to apply community law and to ensure the appliance with community law is the obligation of the Member States. The Commission as the guardian of the Treaty has an exclusive role in the enforcement. It is the task of the Member States to make the measures necessary to ensure the compliance with provisions of the Treaty and fulfil obligations arising from the acts of the community institutions. One element of the cooperation between Member States is that they facilitate the performance of the tasks of the Community, and they will abstain from any acts that would endanger the realization of the aims contained in the Treaty.

In the process of notification the ministry in charge of the preparation of legislative bills for the purpose of approximation without delay notifies at the chief executive level of Ministry of Foreign Affairs and the Ministry of Justice - for the purpose of notification of the European Commission - when a legal act adopted for the purpose of approximation has been published, and indicates the legal the EU legal act with which it is fully in compliance. If the community legal instruments prescribe the notification of the transparency table as well which shows the harmony between the individual provisions of the instruments this table also have to be filed. If the ministry of justice agrees with the position of the responsible ministry, signals this to the ministry of foreign affairs, which procure the electronic version of the legal instrument and makes the notification to the European Commission. In the practice of the original member states the form of the notification is in paper, but it is awaited that after the accession it will be possible to make notifications electronically. It would be more useful to Hungary for reasons of fastness and the easier following with attention of the processes.

As I have already mentioned it is a huge amount of legal instruments to which we had to approximate our laws for being ready for the accession. The acquis is criticised not only in amount but also in quality. The Community has already recognised this problem more than a decade ago,

and the Commission had worked out its first program for the simplification and amelioration of the community law in 1995.\textsuperscript{15} The key words of the Commission communication in 2002\textsuperscript{16} were legislating less but better. This besides stressing the liability of the community institutions notifies that the Member states also has apolitical liability in simplifying and developing community law in a governmental and parliamentarian level as well. The effective and successful transplantation of community legal instruments would in a positive way affect legislation culture of the European union. What could be done by the Member States for better legislation? Firstly they should perform their implementation duties in time. Secondly they should involve their institutions responsible for the transposition and application of directives in the process of legislation. This way precedingly the results of community legislation which require further national implementing measures should be surveyed before their adoption, and public should also be involved in the legislation process. The development of coordination between community institutions and member states would also contribute to a better legislation.\textsuperscript{17}

As a conclusion it can be stated that legal harmonisation process has not come to an end with the accession, it must continue with the utilization of the experiences required in the accession period, it had to be continued with regard to the fact after the accession our failures of harmonisation can have serious consequences, and our most important aim should be to avoid these consequences.

\textsuperscript{15} Commission reports to the European Council’s Better Law-making on the application of the subsidiarity and proportionality principles, on simplification and on consolidation -1995 (CSE (95) 0580-C4-0561/95)

\textsuperscript{16} Commission communication, Action plan simplifying and improving the regulatory environment, 6 June 2002 (COM (2002) 278 final)

\textsuperscript{17} The commission evaluates the acts of institutions and Member States in its reports on better legislation (11th report in 2003. COM (2003) 770)
NEW CHALLENGES IN THE EU LAWMAKING

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Field of research: The role of national parliaments in the institutional system of the European Union

Abstract: The essay attempts to give an overall review of the 'new challenges'- processes and changes- the lawmaking of the European Union faces with following the signing of the Treaty of Nice. Through listing the main documents in this topic, the continuous development of how the needs emerging from the enlargement of the EU and other recent expectations were committed to writing can be tracked step by step and -as a final acknowledgement of the reforms - we can get acquainted with the regulations of the Treaty Establishing a Constitution for Europe that summarizes and works out the up-to-date elements of the decision making of the Union.

The Treaty of Nice\(^1\)- as it is well- known- started but could not satisfactorily finish the sound revision of the legal system of the EU. Recognizing the needs emerging in the field of EU lawmaking-especially those in connection with the enlargement process- a wide range of documents came up targeting the updating of existing legal instruments. These documents have worked out, specified or put into practice the modern requirements of the Community law with a special attention to unfold the basic principles of subsidiarity, proportionality, transparency, the openness of EU institutions, participation etc. The reforms emphasize the importance of both procedural and administrative changes.

The European Commission, when presenting a Communication on its 'Strategic Objectives 2000-2005- Shaping the New Europe'\(^2\) announced the intention to launch a series of important initiatives in the domain of public governance. As regards the lawmaking, the following aims were appointed: giving people a greater say in the way Europe is run; making the institutions work more effectively and transparently, notably by reforming the Commission, which may serve as an example for other bodies and building new forms of partnership between the different levels of governance in the EU. In the same year, the European Parliament (Cashman-report)\(^3\) underlined that trust and confidence in the European Union and its institutions can only be ensured if an open and democratic political debate and decision-making process takes place at all levels. The Charter of Fundamental Rights of the European Union\(^4\) stresses the same concept of openness in Article 41 “right to good administration” and Article 42 “right of access to documents”. The objectives of the Union shall be achieved with respecting the subsidiarity principle.

In deep accordance with these ideas, the Laeken European Council in 2001 formulated a Declaration on the Future of the European Union (which was later enclosed in a shortened form to the Treaty of Nice as a Declaration). It not only stated that there exist serious disfunctions concerning the contact between the citizens and the EU institutions whilst an enhancing of

\(^1\) COM (2000) 154 final-Communication from the Commission to the European Parliament, the Council, the Economic and Social Committee and the Committee of the Regions- 'Strategic Objectives 2000-2005- Shaping the New Europe'

\(^2\) A5-0318/2000 Resolution of the European Parliament

\(^3\) The Charter of Fundamental Rights of the European Union, signed on 04 November 1950
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democracy, transparency and effectiveness of the Union —with a greater involvement of the national parliaments— is unavoidable but at the same time the Declaration established a Convention to prepare the way for a new treaty that would offer a solution to these challenges. It was the recognition that the Treaty of Nice would not be able to perform its ‘mission’.

Summarizing the above mentioned needs, the Commission proposed a White Paper on European Governance, which outlined four main areas of reforms: better involvement and more openness in the decision-making process (by paying attention to the bottom-up initiatives); improving and simplifying Community legislation and widening the choice of legislative instruments to allow for greater flexibility in addressing the Union’s changing needs; clearer delineation of competences between the EU-institutions together with improving interinstitutional dialogue and -at last but not at least- strengthening the unity and coherence of Union’s representation globally. Based on the objectives drafted in the White Paper, the Commission presented its action plan for better lawmaking in different Communications dealing with the regular use of extended impact assessment, promoting a culture of dialogue and participation (offering minimum standards for the consultation with the interested parties and experts) and outlining the simplification and improvement of the regulatory environment—that means a guarantee that the reasoning behind the legal proposals are clear and that the documents fulfil the requirements originating from the principles of subsidiarity and proportionality.

A great step was taken towards the openness of decision-making when the European Parliament and the Council set a common Regulation regarding public access to European Parliament, Council and Commission documents. This Regulation defined general rules and conditions (including certain deadlines) of how the people or other EU institutions can obtain a certain EU document.

At its 2002 summer meeting in Seville, the European Council requested the Council of Ministers to adopt measures so that to improve the transparency and efficiency of the Council’s decision making process. For the sake of this, a long term planning became due and a more effective co-operation between the successive Presidencies. Each December, the European Council has to draw a tri-annual strategic programme together with an annual operating programme of Council activities, which appoints the indicative agenda for the Council meetings. A new Council format was created (‘Council of General Affairs and External Relations’), simultaneously with a radical abatement of the existing formats (from 15 to 9). The Council’s Rules of Procedure was thoroughly modified: when, for instance, the co-decision procedure is applied, the discussion of the legal proposals are fully opened, including the working documents, final acts and the reasons of voting.

In June of 2002 the Commission proposed an ‘Action Plan on Better Regulation’ with a call for making the EU legislation more targeted and with a desire to lead in minimum standards of consultation between the EU institutions and the population when shaping the common policies. No

6 COM (2002) 276(01)- Communication from the Commission on Impact Assessment
8 COM (2002) 278(01)- Communication from the Commission - Action plan on ‘Simplifying and improving the regulatory environment’
10 Decision 10962/02/EC of the Council, 19 July 2002 on adopting the Council’s Rules of Procedure
11 (Operative) Treaty Establishing the European Community, Article 251
sooner after that, a debate on the reform of the so-called ‘comitology system’ started its way, concerning among others the issue of parliamentary overview in the supervision of implementing procedures.

A couple of months later, on the 20th of November, 2002 the Council and the European Parliament signed an inter-institutional agreement that regulated the access of the EP to third pillar confidential information.

An outstanding result of this year was the introduction of the integrated impact assessment. This system replaced the previously separated assessments to a single template that evaluates the social, economic and environmental aspects of legislative proposals and those non-legislative proposals or initiatives that have such impact (including White Papers, negotiation guidelines for international agreements, the proposals of the Annual Policy Strategy etc.). The above mentioned system will be fully operational in 2004-2005 and will substitute the earlier examinations, except for ex-ante evaluations of programmes resulting in expenditure from the general budget of the EU. The Commission has conducted 43 extended impact assessments on proposals from its 2003 Work Programme and has also identified 41 proposals for this year that will undergo extended impact assessments. The assessment itself starts with a preliminary stage that acts as a filter- the Commission then selects, which proposals will result in substantial economic, environmental and/or social impacts or whether the proposal represents a major policy reform. If the proposal meets these requirements, an extended assessment follows, a more in-depth analysis, which involves consultation with experts and interested parties.

Following the European Council meeting in Brussels, an Interinstitutional Agreement on Better Lawmaking was signed between the European Parliament, the Council and the Commission (December 2003). Its main initiatives were as follows: a better coordination of law-making procedures, greater transparency, the use of alternative legal tools, a strict indication of the legal basis of the proposals (pointing out the principle of subsidiarity and proportionality), improving the consultation and impact assessment prior to pass an act and decreasing the volume of lawmaking at the Communities’ level. The coordination is of great importance as the lawmaking programme of the Commission and the multi-annual programme of the Council are not always congruent. Where there is a latitude, that is, the Treaties or the common aims do not require the Community’s obligation to legislate, alternative methods of regulation might be used: ‘co-regulation’ and ‘self-regulation’, if they serve the common interests- in accordance with the acquis communautaire- and do not offend the criterion of transparency. In the case of co-regulation, a Community legislative act entrusts the attainment of the objectives defined by the legislative authority to parties which are recognised in the field (such as economic operators, social partners, non-governmental organisations or associations). Self- regulation means a possibility for the above mentioned individuals or legal entities to adopt amongst themselves and for themselves common guidelines at European level (particularly codes of practice or sectoral agreement).

### 1. Reforms of lawmaking in the Constitutional Treaty of Europe

The Constitution of the European Union (which has been signed recently in Rome) incorporates the results and desiderata of the listed documents. It reacts upon the White Book on Better Governance,
especially in the Article on the Transparency of the proceedings of Union institutions\textsuperscript{17} and the Article targeting a better governance on the global level\textsuperscript{18}. A similar Article is the I-5 that regulates the relations between the Union and the Member States (including the role of local and regional self-governments), the I-45 on the principle of representative democracy and its "twin brother", I-46 on the principle of participatory democracy.

The Title III (Part I) separates the Union competences (that was not succeeded in the Treaty of Nice). It raises the principle of conferral\textsuperscript{19} to be the main principle of bounding the competences between the Member States and the EU, while on the practicing of competences the principles of subsidiarity\textsuperscript{20} and proportionality\textsuperscript{21} prevail. The principle of conferral means that competences not conferred upon the Union in the Constitution remain with the Member States. The definition of the principle of subsidiarity was widened: if an objective cannot be sufficiently achieved by the Member States or at a regional and local level, then comes the Union level. The principle of proportionality was unambiguously detached from the principle of subsidiarity but on the use of these two principles there exist a single Protocol in the Constitutional Treaty\textsuperscript{22}. This Protocol orders that the Commission shall not only consult widely on the proposed acts but it also has to justify the proposal with regard to both principles, confirmed by quantitavie and qualitative indicators, if possible.

The control role of national parliaments is fixed partly in the foregoing Protocol, partly in the Protocol on the Role of National Parliaments in the European Union. Simultaneity means that the national parliaments shall obtain the proposals of the Commission at the same time as the Union legislators. Any national parliament or any chamber of a parliament may, within six weeks from the date of transmission of the Commission’s legislative proposal, send to the EU bodies a reasoned opinion stating why it considers that the proposal in question does not comply with the principle of subsidiarity, thus practicing an 'ex-ante' control. The European Parliament, the Council of Ministers and the Commission 'shall take account’ of these opinions, that is in itself not a satisfactory guarantee- but if the national parliaments votes so (see its conditions in the Protocol), the Commission has the duty to review its proposal. Still, the Commission may maintain the original version but must give an adequate reason for that (so this rule does not go too far limiting the powers of the Commission, which have to fight sometimes for the EU’s interests against the particular interests of the Member States). The Member States, national parliaments and chambers (and in a limited scope, the Committee of Regions)- as an ultimate mean- may hand in a claim at the European Court of Justice if they affirm that an act infringes the principle of subsidiarity.

The Article I-10 explicitly states the primacy of the EU law over the national law (earlier it existed in the form of a principle derivated from a judgement of the European Court of Justice\textsuperscript{23}). The Articles I-11 to I-17 act as milestones because they clearly separate the competences of the Member States and the EU. The Union enjoys an exclusive competence (I-12) in only few fields whereas there is a greater number of areas of shared competence (I-13). The EU shall adopt measures or initiatives to ensure the coordination of economic, employment and social policies (I-14). Supporting, coordinating or complementary actions can be proposed at EU level, even if the area defined in the Article I-15 virtually belongs to the single state’s inner law. The flexibility clause still requires unanimosity from the Council if it is substantial to provide the Union with additional powers to attain the aims of the Constitution (I-17).

\textsuperscript{17}Part I Article 49
\textsuperscript{18} Part III Article 193 (2)
\textsuperscript{19} Part I Article 9 (2)
\textsuperscript{20} Part I Article 9 (3)
\textsuperscript{21} Part I Article 9 (4)
\textsuperscript{22} ‘Protocol on the Application of the Principles of Subsidiarity and Proportionality’ annexed to the Constitution of Europe
\textsuperscript{23} See C-6/64 Costa v. E.N.E.L. case
The Title V of Part I – in the name of simplicity and uniformity- sets a smaller number of legal means in comparison to the present ones (I-32), these are the European laws, European framework laws, European regulations, European decisions, recommendations and opinions. A European law is more or less equal to the current 'regulation', while the European framework law is similar to the existing 'directive'. But the European regulation will be a non-legislative act meant to help the implementation of the legislative acts and of certain provisions of the Constitution. It can either be binding or have a nature of the European framework law. The European decision is also a non-legislative act, binding, however, in its whole entirety. A Decision which specifies those to whom it is addressed shall be binding only on them. Recommendations and Opinions adopted by the Institutions have no binding force.

Pursuant to the Article I-33, the lawmaking procedures will go through a radical change. The 'usual' way of law making will be the codecision procedure- confessing the European Parliament as an equal partner in decision making- so the number of areas covered by this procedure will exceed the eighty. The hegemony of the Commission will crack- one quarter of the Member States will also be entitled to inaugurate a legal proposal regarding the agriculture, fisheries and environment policy (III-165). What is more, at least one million citizens coming from a significant number of Member States may invite the Commission to submit a proposal when they consider that a legal act of the Union is required for the purpose of implementing the Constitution (I-46).

The Protocol on the Role of National Parliaments in the European Union highly respects the importance of state parliaments. It ensures the conditions of a proper national scrutiny including enough time for bringing it about and the right to access the widest range of documents are born in the process in lawmaking. This specification is capital since the 'fast-track' lawmaking of the EU jeopardizes the legitimacy and democratism of the EU law. Claus Larsen- Jensen, Chairman of the European Affairs Committee in the Danish Parliament pointed out [Larsen-Jensen 2004.] that one third of the proposals are accepted in the first reading of the codecision procedure, therefore the national parliaments have to have the relevant information as soon as it is possible to form their standpoint. As the codecision procedure is often accompanied by so-called trilog agreements [Larsen-Jensen 2004.], where a member of the Council Presidency, the rapporteur or the chairman of the relevant EP-Committee and a representative from the Commission make an informal agreement on the fate of the proposal in question, the exact rules of these agreements are also have to be worked out and the national parliaments have to be informed on these meetings, too.

2. Summary

As we could see, the sources of law and the lawmaking system are also in basical changing. The influence of numerous documents- interinstitutional agreements, resolutions, White Papers etc.- can already be observed in the practice of today’s. The most up-to-date proposals usually contain a reference to the principle of subsidiarity or proportionality (even if in my experience these references simply repeats the Article 5 of the updated Treaty of Rome24) and these principles are ‘beloved’ in plaints addressed to the Court of Justice. There was no example before to involve such a broad publicity in making a proposal, for example the proposed text of the so-called ’REACH-regulation’25 was placed on the internet and some 6000 suggestions arrived in return from civil organizations, social partners, member states etc., which lead to an amendment of the proposed text, making it significantly more cost-effective. The use of financial impact assessments are quite widespread and the reasoning of the memoranda of proposals are becoming more and more complex: let

24 Treaty Establishing the European Community, signed on 25 March 1957
me mention the proposal for a new working time directive that adduces to several aspects of the question, from the Lisbon Strategy to the Charter of Fundamental Rights of the Union or the opinion of the social partners and advisory bodies. The involvement of national parliaments to the decision-making is ensured by the New Convention but a factual better cooperation can already be observed between the parliaments and EU institutions: for example, the number of meetings of the counterpart committees of the EP and the national parliaments has quadrupled, rising from 10 in 1998 to 40 in 2002.

There are much more (electronic) EU database than a couple of years ago and their accessibility has become easier as for instance the CELEX site has been free of charge since July 2004 and the user’s applications and the contained documents have been continuously translated into the official national languages. The Commission regulatory reports its scoreboards on the implementing of directives in the different Member States- although the infringement cases rarely get to the Court of Justice, the warning of the Commission is usually effective enough for a Member State to apply the questionable directive.

The Constitutional Treaty in its complexity mirrors the criteria of simplicity, participation and transparency, fixes in details the competences of the decision-makers and offers guarantees to control the principles of lawmaking. The growing number of decisions taken by a qualified majority do threat, however, the democracy of lawmaking (as it is unavoidable that sometimes the interests of a Member State- in lack of allies- will be voted down). At last, I would like to call the attention to a phenomenon excellently illustrated by the EU Constitution (especially by building the whole Charter of Fundamental Rights of the European Union to its text), namely that there is also a turn in the content of the legal acts: the progressive social ideas –like gender equality- appear in directives and regulations, making the EU- within the frames of economic rationality- sensitive to values and committed by the improvement of the quality of life.

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DEFINITION OF COMPARATIVE ADVERTISING

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Abstract: This study divided into three parts. First chapter tries to show the economic function of the comparative advertising, its risks, interests to be protected and the main features of its regulation. The second part is about the definition of comparative advertising. A new draft directive is analysed in the third chapter as a possible solution to create two kinds of comparative advertising. In the summary the author tries to shortly assuming main ideas of the study and gives some remarks and critics.

I. Comparative advertising in general

Before analysing the definition of comparative advertising useful to show the comparative advertising in general.

Comparative advertising, as a special form of advertising, is a sales promotion device that compares the products or services of one undertaking with those of another, or with those of other competitors. All comparative advertising is designed to highlight the advantages of the goods or services offered by the advertiser as compared to those of a competitor. In order to achieve this objective, the message of the advertisement must necessarily underline the differences between the goods or services compared by describing their main characteristics. The comparison made by the advertiser will necessarily flow from such a description.

1. Function of comparative advertising

Comparative advertising should enable advertisers to objectively demonstrate the merits of their products. Comparative advertising improves the quality of information available to consumers enabling them to make well-founded and more informed decisions relating to the choice between competing products/services by demonstrating the merits of various comparable products. Based on this information, consumers may make informed and therefore efficient choices. (These statements are true only if the comparative advertising is objective.)

Comparative advertising which aims to objectively and truthfully inform the consumer promotes the transparency of the market. Market transparency is also deemed to benefit the public interest as the functioning of competition is improved resulting in keeping down prices and improving products. Comparative advertising can stimulate competition between suppliers of goods and services to the consumer's advantage.
2. Risks of comparative advertising

Comparisons between goods and services of different undertakings carry with them some significant risks. There is a danger that once undertakings address the merits and inadequacies of competing goods or services, they may be tempted to denigrate them or derive unfair advantages from such inaccurate comparisons. Just like traditional forms of advertising, comparative advertising seeks to both assist the development of the undertaking concerned and to inform consumers. Although both forms of advertising seek to attract customers, in case of comparative advertising, commercial relationships may be exposed to the constant threat of unfair practices.

3. Interests

3.1. Affected interests

Comparative advertising affects the interests of consumers as well as the interests of competitors, interests of proprietary rightholders and, in this way, those of the general public. Possible harm of interests of consumers and interests of competitors is obvious, but there is a need to show the role of proprietary rightholders. Proprietary rightholders have a trade mark or a trade name. This trade mark or trade name is used by advertiser in comparative advertising. In order to make comparative advertising more effective, it is useful for the advertiser to identify the goods or services of a competitor, making reference to a trade mark or trade name (hereinafter together trade mark) of the proprietor. However, the holder of a trademark has the exclusive right to use it to identify the products or services for which the trademark is registered, and to dispose thereof. The scope of the exclusive rights conferred by trademark protection covers the right to use the trademark for advertising purposes.

Proprietary rightholders are in a lot of cases same persons as competitors, but they create a smaller group of persons inside competitors. Sometimes proprietary rightholders are different persons than competitors, their product or service is not a competitive one to advertiser’s product or service.

3.2. Interests to be protected

The interests to be protected by the law are the following:

- the protection of competitors;
- the protection of proprietary rightholders;
- the protection of consumers; and
- the protection of the general public interest in undistorted competition.

(i) Due to the special characteristics of comparative advertising, namely the direct or indirect reference in the advertising to identifiable competitors, it is important to protect the interests of such competitors as well in order to prevent disparagement, or taking of unfair advantage of the competitor's reputation. This consideration justifies the application of the general rules on unfair competition very thoroughly and – where necessary – the application of special conditions that comparative advertising should comply with in order to ensure that unfair use of the competitor’s reputation and disparagements of competitors be prevented.

(ii) As far as the proprietary rightholders are concerned the cases are related to the use of well-known trademarks or trademarks enjoying good reputation. Obviously, the affected trademark must have a reputation in the market for the products or services provided. This reputation can economically be exploited. Trademark owners must have enjoy a wider scope of protection against taking unfair advantage of the reputation. In these cases, consumers may more easily associate the products formulas with a well-known trademark.

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1 The function of the trademark is to individualize and distinguish products or services.
Comparison of Comparative Advertising

Definition of Comparative Advertising

- In a ‘classical’ comparative advertising the advertiser compares its product or service to competitor’s one, using its trademark during the comparison. The aim of competitor is to evidence that its product or service is better than the competitor’s one. In my opinion there is a significant difference between correct and incorrect comparison. A falls statement affects the interests of consumer as well as the interests of competitor (as a potential market looser) and interests of proprietary rightholder (because the value of its trade mark can be reduced). Competitor and proprietary rightholder in this case is the same person. The falls comparison poses two types of harms to the same person: to the competitor (as a potential market looser) and to proprietary rightholder (because the value of its trade mark can be reduced).

Even a true statement can be considered as illegal to a proprietary rightholder. In this second case the comparative advertising does not affect the competitor’s goodwill, but the frequently using of its trade mark can be stated as unfair. Even correct and objective advertising may be considered unfair when it exploits the renown of a competitor by attributing to his own product the well-known qualities of the product of the competitor. The exploitation of the reputation of a competitor is admissible when it enhances the transparency of the market and is limited in form and content to what is necessary for this purpose (principle of proportionality). Hence, a company should refrain from referring to its competitors and use their trademarks, except in case of absolute necessity.

- The advertiser gives the impression that he is advertising for the goods of the trademark owner instead of for his own goods.

- The use of a third party’s trademark in advertising can mislead the public about the existing relationship between the advertiser and the owner of the trademark.

- The advertiser refers to the famous trademark or distinctive sign to take advantage of its renown and to favour its own product which it describes as being as good. The two products are not contrasted with each other (as in the first example), but described as being both as good. When the reference to others’ trademark is combined with words such as “in the style of … “, “type”, the “kind”, a risk of confusion may appear since the public does not take such words into account. With respect to the use of trademarks in comparative advertisements, it is not allowed to take unfair advantage of their reputation by way of assimilation. It was considered to contravene public policy, if the advertiser tries to show the quality of its own products by comparing them to well known other products in order to make use of their standing and reputation. Using trademarks unfair way in comparative advertising is parasitism, i.e. the exploitation of others’ reputation. So-called "parasite" advertising takes advantage without restraint of the good reputation of a competing or non-competing product.

(iii) Potential misleading nature of the comparative advertising is the main danger for consumers. Pursuant to Article 2 (2) of Directive 450/84, an advertisement is misleading if ‘in any way, including its representation, it deceives or is likely to deceive the persons to whom it is addressed or whom it reaches and if, by reason of its deceptive nature, it is likely to affect their economic behaviour or, for those reasons, injures or is likely to injure a competitor.’ Whether a comparative advertisement is misleading or not, depends on the understanding of the relevant public. The standard is an average consumer who is reasonably well-informed. A comparative advertisement would be misleading.

2 One Austran case involved a comparative advertising campaign of a major Austrian drugstore, where several products of the drugstore’s newly established house-brand were compared with well-known competing brand products (for example, “Kodak”). The advertisements only highlighted the – substantially – lower price of the drugstore’s own products without establishing why the compared products can be seen as equal. Almost similar factual pattern relating to well-known perfumes happened even in Hungary.

3 Relevant public is created by people to whom the advertisement is addressed or whom it reaches.
therefore forbidden, if certain part\textsuperscript{4} of the relevant public – consisted reasonably well-informed consumers – would be mislead. Price comparisons are especially dangerous. Stating alonely the cheaper price is can be misleading to the consumer, if the difference in price is due to fact that the more expensive product or service meets ore needs or has more advantages.

A further possible danger of the comparative advertising for consumers is the confusion. A correct comparative advertisement does not create confusion between the advertiser and its competitor.\textsuperscript{7}

(iv) Having regard a Member State legislation it cannot be established whether in case of comparative advertisements, the protection of the general public interest in undistorted competition constitutes an independent interest to be protected or this is an aggregate result arising from the protection of consumers, competitors and rightholders. For the EC is very clear the independent importance of general public interest, namely strengthening of the internal market and limiting gaps of free movement of goods and services (see 5.1.).

4. Different European attitudes

Comparative advertising as a kind of advertising has a long history, but as a legal term relatively young phenomenon. Before 1970 ‘comparative advertising was not regulated because it was regarded as insider question of competitors, and it was supposed that rules of competition law offer adequate protection’.\textsuperscript{5} Lack of specific regulation leaded to the practical prohibition. Comparison in an advertisements generally was regarded, as an illegal market practice.

The American court practice realised first that comparative advertising is a complex, difficult activity having a lot of speciality. While in the United States comparative advertising has been a well-recognised and acceptable form of advertising, Europe was divided in this point of view. There were a significant difference in Europe in the Seventies. The majority of European countries have been hostile to such advertising for a long time and this form of advertising was considered as a per se unfair market practice. The comparative advertising was held too risky and dangerous in most of the continental countries. This method of advertising was prohibited by the general rules of unfair competition law, without special legal norms. Imre Vörös shows the traditional Germain prohibition.\textsuperscript{7} ‘The UK has a relatively liberal regime permitting comparative advertising in most cases but in many continental countries all comparative advertising, even if true, has been classed as unfair competition or automatically misleading.’\textsuperscript{8} In the United Kingdom and in Portugal the comparative advertising became legal.\textsuperscript{9} I have to add, that this liberalisation was relative, comparative advertising even in England was accepted only in certain circumstances. Articles 20-24 of the British Code of Advertising Practice\textsuperscript{10} contained detailed suggestions for comparison in advertisements. Later accepted rules of EC Directive (see 5.1.) are similar to these suggestions, so in

\textsuperscript{4} Directive does not use the “certain part of the public” phrase, but Member States’ laws or court practices require more than one mislead consumer: 10-15 % of the public in the Swiss law, or ‘a substancial proportion of the reasonable audience’ (UK).

\textsuperscript{5} Some examples of confusion: consumer became uncertain to whom belongs tarde marks, whether the advertiser is a subsidiary of the other company or not and so one.

\textsuperscript{6} Pribula László: A reklámtevékenység és a reklámszerződések hazai jogi szabályozása PhD disszertáció Debrecen 2003., kézirat 91. p

\textsuperscript{7} Vörös Imre: Az európai versenyjogok kézikönyve TRIORG Kft., Budapest 1991. 28 p

\textsuperscript{8} Howard Johnson: New EU directive on comparative advertising Tolley’s Communications Law Vol 3 Number 2 1998. 66. p


\textsuperscript{10} The British advertising industry has a system of self-regulation which has been established under the auspices of its voluntary regulatory body, the Advertising Standards Authority (ASA). There is a British Code of Advertising Practice which is administered by the code of advertising practice committee, and the committee and the ASA deal with complaints of breaches of the code.’ Miller-Harvey-Parry: Consumer and Trading Law Oxford University Press, Oxford 1998. 533 p
my opinion that these, non obligatory, rules of the British Code of Advertising Practice were a kind of pattern for the European legal harmonisation work. Telling me the trough the correct comparison even in UK was not absolutely free. The English Trade Marks Act (1938) prevented much comparative advertising not allowing competitors to use registered trade marks without the consent of the right owner.11 Even 'the criteria in Member States where comparative advertising is permitted differs in several ways'.12

A kind of convergence started in the late Seventies’ in UK and continued in Germany in the Eighties’. In the English court praxis have arrived cases when a comparative advertising created a ‘passing-off’. Falls statement that the advertiser’s movie is based on somebody else’s successful novel was accepted as a passing-off by the court.13 In 1979 a new tort was created. The tort of unfair competition in certain cases covered even the comparative advertising. Seller’s falls statement about that its products are better than its competitor's products harms the competitors goodwill.14

In the Germain Law the price-comparing became legal in 1988, except it is contrary to the business fairness.15

Presented examples on convergence do not effect the fact that Europe was divided in the point of view of acceptance on comparative advertising. This situation closed a lot of problems.16 So the EC legislation (see it in 5.) was a great step forward.

5. EC regulation on comparative advertising

5.1. Legality of comparative advertising

Comparative advertising is considered by the European Union as a legitimate means of informing consumers of the advantage of the product or service compared with that of a competitor. The EC accepted the comparative advertising both by the legislation both by the court practice.


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11 Prohibition was cancelled only in 1994. Section 10(6) Trade Marks Act 1994 now allows the use of a competitor’s trade mark provided the use is (i) in accordance with 'honest practices in industrial and commercial matters, and (ii) not 'without due cause taking unfair advantage of or being detrimental to the distinctive character of the trade mark'.

12 Advertising and the consumer within the European Community, EC Consumer Information programme Kestrel Communications, London 1993. 21 p

13 Samuelson v. Producers Distributing Co. Ltd. 48 RPC 593


15 See more detailed way in Vörös Imre: Az europái versenyjogok kézikönyve 2. kiadás Logod Bt., Budapest 1996. 12 p

16 Numerous users of commercial communications also complain that they cannot use comparative advertising in certain Member States, and are therefore forced to redesign entirely their commercial communication campaigns in those territories. The complaints focus on Germany, Belgium, France and the Netherlands. On this, the Commission has proposed that comparative advertising should be permitted as long as it is based on objective comparsons that are not used to denigrate the trademark or reputation of a competitor. At the level of Council, political agreement on this proposed directive was reached in November 1995. Commercial Communication in the Internal Market – Green paper from the Commission Brussels, 08.05.1996., COM(96) 192 final.


18 Following the adoption of Directive 97/55 all EU member states have introduced the comparative advertising into the national legal systems.

In my opinion there were three reasons to accept the comparative advertising by the European legislation.
First - more theoretic – base for the legalisation this kind of advertising was a constitutional one: the freedom of speech. In business, the constitutional (fundamental) principle regarding freedom of speech is inextricably intertwined with the freedom of advertising. Secondly was to ensure free movement of advertisements as a service.
Third – more practical – basis was strengthening the insider market. Advertising is a typical cross-borderer activity. Different national attitudes: the acceptance or non-acceptance of comparative advertising in the various national laws, may constitute an obstacle to the free movement of goods and services and create distortions vis-à-vis of competition.
Fourth reason was strengthening the competition in insider market. True and not misleading comparative advertising is a useful instrument for acquisition of market at competitors’ costs. This competition-related reason became more powerful in decisions the European Court of Justice (ECJ).

Acceptation the comparative advertising looks like contrary to the consumer protection. The European Parliament and the Council defined a lot of requirements to protect consumers (see 5.2.).

(ii) The European Court of Justice (ECJ) and the Court of First Instance have interpreted the meaning of certain provisions of the Directive in three cases. These decisions have great importance in clear understanding of requirements (see 5.2.) for legal comparative advertising. The Piping case in my opinion helps to understand the real place of comparative advertising. The European Court of Justice held that ‘the Directive carried out an exhaustive harmonisation of the conditions under which comparative advertising in Member States might be lawful. Such a harmonisation implies by its nature that the lawfulness of comparative advertising throughout the Community is to be assessed solely by the criteria laid down by the Community legislation. Therefore, stricter national provisions on the protection against misleading advertising cannot be applied to comparative advertising with regard to the form and content of the comparison.’ This Decision clearly shows that the EC comparative advertising legislation is mainly belong to the internal market. In my opinion strengthening of the free movement of goods and services was much more important for the European Parliament and the Council, than the consumer protection. Consumer protection legislation is a minimum harmonisation. Member States has right to adapt stricter rules, they can provide a higher level protection for consumers, than the European Directives. Member Stets have no similar

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20 Pursuant to Article 10 of the European Convention on Human Rights (Rome, 1950), every person has the right to freedom of expression. This right shall include freedom to hold opinions and impart information and ideas without interference by public authority. The exercise of these freedoms, since it carries with it duties and responsibilities, may be subject to such formalities, conditions, restrictions or penalties as are prescribed by law and are necessary in a democratic society … for the protection of the reputation or the rights of others. (This limitation has an important role in case of comparative advertising.)

21 "Advertising is an important element of the competitive situation on any given market, since it provides a better picture of the merits of each of the operators, the quality of their services and their fees. Furthermore, when it is fair and in accordance with the appropriate rules, comparative advertising makes it possible in particular to provide more information to users and thus help them choose a professional representative int he Community as a whole whom they may approach. Consequently, a simple prohibition of comparative advertising restrict the ability of more efficient professional representatives to develop their services, with the consequence, inter alia, that the clientele of each professional representative is crystallised within a national market.” (Judgement of the Court of First Instance of 28 March 2001. Institute of Professional Representatives before the European Patent Office v Commission of the European Communities, Case T – 144/99., 72-74)

22 Three cases can be mentioned by the European Court of Justice (ECJ) and the Court of First Instance as interpreting – and developing in my understanding - the Directive: (i) Case C-112/99, Toshiba Europe GmbH v. Katun Germany GmbH, 25 October 2001; (ii) Case C-44/01, Pippig Augenoptik GmbH & Co. KG v. Hartlauer Handelsgesellschaft mbH, 8 April 2003, and (iii) Case T-144/99, Institute of Professional Representatives before the European Patent Office v Commission of the European Communities.

23 Court decisions are not analysed in this study because they conected mainly to the requirements of the comparative advertisement, but my topic is the definition of the comparative advertising.

24 Case C-44/01
right connected to the comparative advertising.\textsuperscript{25} This is the main evidence that legislation on comparative advertising is not a part of consumer protection. These topics are connected, but comparative advertising is larger than protection of consumers against misleading advertising. There are other protecting interests (as you could have seen in 3.) too, and legal methods are different.

5.2. Legal requirements

5.2.1. Regulation on misleading advertising
Comparative advertising should comply with restrictions applicable to all advertisements: that is, it shall not cause confusion, mislead, or discredit a competitor.\textsuperscript{26} Due to the special nature of comparative advertising, however, certain additional requirements should be applied to this type of advertising (see 5.2.2.).

5.2.2. Additional rules for comparative advertising
Comparative advertising is a legitimate means of informing consumers of the advantage of the product or service compared with that of a competitor. In order to guarantee that it fulfils this objective, comparative advertising must be used in a fair manner. It is important to establish special criteria for objective comparisons and rules with regard to the possibility to compare products and services.

There are positive requirements (i.e., the objective comparison of material, relevant and verifiable features of the goods) and negative requirements (i.e., not to be misleading, not causing confusion, not discrediting the competitor) which comparative advertising should comply with.\textsuperscript{27}

6. Equivalent requirements in Member States

6.1. Legality of comparative advertising
All the EU countries have implemented the Directive in their legal systems. Comparative advertising is generally permitted, however, subject to certain circumstances set forth in the national law.

6.2. Legal requirements
In the continental European countries\textsuperscript{28} the rules on comparative advertising are based on statutory law, although the interpretation of such rules have been developed by the court practice, in certain

\textsuperscript{25} General rules for unfair competition does not provide sufficient legal certainty and leaves too wide a scope for divergence of national laws and jurisprudence which would hinder cross-border trade. So additional requirements should be applied to comparative advertising.

\textsuperscript{26} Directive 84/450/EEC concerning misleading advertising

\textsuperscript{27} Pursuant to Article 3(a)(1) of the Directive, comparative advertising shall, as far as the comparison is concerned, be permitted when the following conditions are met:

(a) it is not misleading;
(b) it compares goods or services meeting the same needs or intended for the same purpose;
(c) it objectively compares one or more material, relevant, verifiable and representative features of those goods and services, which may include price;
(d) it does not create confusion in the market place between the advertiser and a competitor or between the advertiser’s trade marks, trade names, other distinguishing marks, goods or services and those of a competitor;
(e) it does not discredit or denigrate the trade marks, trade names, other distinguishing marks, goods, services, activities, or circumstances of a competitor;
(f) for products with a designation of origin, it relates in each case to products with the same designation;
(g) it does not take unfair advantage of the reputation of a trade mark, trade name or other distinguishing marks of a competitor or of the designation of origin of competing products;
(h) it does not present goods or services as imitations or replicas of goods or services bearing a protected trade mark or trade name, and
(i) any comparison referring to a special offer shall indicate in a clear and unequivocal way the date on which the offer ends or, where appropriate, that the special offer is subject to the availability of the goods and services, and, where the special offer has not yet begun, the date of the start of the period during which the special price or other specific conditions shall apply.
countries by arbitration. In addition to statutory rules, there are professional codes and industry self-regulation rules relating to comparative advertising.

6.2.1. Requirements developed by statutory law

The admissibility of comparative advertising will be examined in the light of the criteria set forth in the Directive. Recital (11) of the Directive provides that the above listed conditions for comparative advertising should be cumulative and should be respected in their entirety. Further, the ECJ held that the Directive carried out an exhaustive harmonisation of the conditions under which comparative advertising in Member States might be lawful. Therefore, stricter national provisions on the protection against misleading advertising cannot be applied to comparative advertising with regard to the form and content of the comparison.29

National legislation’s have no right to develop additional criteria for the admissibility of the comparative advertising comparing the Directive. However, there are certain further criteria applicable with respect to certain goods and/or services or set forth in professional codes and/or industry self regulation rules relating to comparative advertising.

6.2.2. Provisions in professional codes of conducts and/or industry self-regulation

In some30 countries, in certain fields of business or industry (pharmaceutical industry, consumer credit), the legislators enacted special rules on the admissibility of comparative advertising.31 Special rules applicable to comparative advertising in certain fields of business (i.e., media, the toys industry, investment banking, pension funds, pharmaceuticals, professional services, and within lawyers), in addition to the general rules on advertising restrictions, can be found in self-regulatory code of conducts.32

Legal or illegal nature of these rules must be decided on the base of partly Directive, partly other European norms.

(i) Article 7 (5) of the Directive provides that nothing in this Directive shall prevent Member States from, in compliance with the provisions of the Treaty, maintaining or introducing bans or limitations on the use of comparisons in the advertising of professional services, whether imposed directly or by a body or organisation responsible, under the law of the Member States, for regulating the exercise of a professional activity.

(ii) With respect to the requirement of "in compliance with the provisions of the Treaty", in Case Institute of Professional Representatives before the European Patent Office v Commission of the European Communities33, the Court of First Instance of the European Communities held that the provisions of the code of conduct by prohibiting advertising comparing professional representatives, constitute restrictions of competition for the purposes of Article 81 EC, thus, Article 7 (5) of the Directive does not exempt in itself such rules from the provisions of the Treaty.

28 In the United Kingdom, the rules on comparative advertising are a mixture of statutory law and case law.
29 Case C-44/01, Pippig, para 44
30 In other countries (the Netherlands) there are only such product or service specific requirements that often include an obligation to provide certain information but these would apply to all advertising.
31 It shall be noted that in the UK, it is a criminal offence for anyone to issue an advertisement which suggests that the effects of a particular medicinal product intended for human use are better than, or equivalent to those of an identifiable treatment or medicinal product.
32 Generally, the self-regulatory rules are only binding for the members of each association. In some cases membership is compulsory for professionals (i.e., for lawyers, in the corresponding Bar Association).
33 Case T-144/99
### 7. Hungarian regulation

There is no place to analyse the Hungarian regulatory history of comparative advertising, but I have to mention that this topic had high level regulation in Unfair Competition Act in 1984. At that time this method was forbidden in the most continental countries and EC only planned to regulate this problem (Directive was created only 13 years later).³⁴

Today, similarly to other Member Stets’ solutions, comparative advertising is generally permitted, however, subject to certain circumstances set forth in the national law. Construction of the regulatory work is also very close to the Western-European patterns.

(i) The rules on comparative advertising are defined by statutory law, in specific rules, in addition to the general rules on unfair competition. Main rules belong to advertising law³⁵, but they are in strong correlation with the competition law rules³⁶ Interests of competitors as well as those of consumers are protected by both Acts.

(ii) Case law is relatively well developed on comparative advertising. There are a lot of interesting cases in Hungarian court practice.³⁷

(iii) The present Hungarian Code of Advertisement-Ethics (2001) contains a brief rule.³⁸ Moreover, the beer industry has a Code of Advertisement-Ethics, and the tobacco industry a Self Regulating Agreement. The self regulating rules laid down in these Codes are binding for the market participants of the given industry. They cannot be enforced, but having authority in the relevant industry, reference is made to them from time to time in decisions of the Competition Council or of the Courts.

### II. Definition of comparative advertising

Legal literature³⁹ is heavily concentrated to show and partly to analyse the requirements of comparative advertising, its definition looks like a second range question. This topic generally is missing from books and articles. In my opinion it is important to determine the comparative advertising firstly because only this type of comparison can be regarded as lawful in certain circumstances, secondly because in this case legal requirements mast been followed.⁴⁰

#### 1. Legal definition of comparative advertising

This study concentrates to the European definition.⁴¹ Pursuant to Article 2a. of the Directive, ‘comparative advertising means any advertising which explicitly or by implication identifies a competitor, or goods or services offered by a competitor.’ Recital (6) of the Directive 97/55 sets forth that it is desirable to provide a broad concept of comparative advertising in order to cover all types of comparative advertising.

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³⁵ Act No. LVIII of 1997
³⁷ For example: ‘Auchan is the cheapest – Tesco is the most expensive’ Vj-209/2000
³⁸ Art. 5 (13) of the Hungarian Code of Advertisement-Ethics is very brief and it provides that: “The data offered in comparative advertisements must be impartial and suitable to be proved with an unambiguous and professional examination.”
⁴⁰ Outside of comparative advertising requirements listed in Directive have no real legal importance.
⁴¹ Hungarian definition of comparative advertising is in 3.
1.1. Identification

1.1.1. Identification of a competitor

Comparative advertisements is not only about the advertiser, but about an other legal or natural person. It is not required to expressly mention the name of the competitor in the comparative advertising. There are several different ways to identify a competitor in a comparative advertisement or, even if the competitor's name is not mentioned. However, it must be clear that the competitor is affected by the statement; therefore, such reference must be clear and unmistakable, and must establish in any manner a link between two persons (i.e. advertiser and its competitor).

1.1.2. Identification of goods or services offered by a competitor

Comparative advertisements is not only about the advertiser products, but about goods or services offered by a competitor. Similarly to the identification of a competitor in this case comparative advertisements must establish in any manner a link between the goods or services of the advertiser and the goods or services of one or more competitors.

1.2. Methods of identifying the competitor or its product

There are several different ways to identify a competitor or its product in a comparative advertisement. Such reference can be made directly or indirectly. ‘Attempts to limit comparative advertising to only explicit advertising were ultimately rejected.’

Any reference made to the competitor or its goods or services, explicitly or implicitly, is considered to be comparative advertising.

It does not make any difference whether the comparison is direct or indirect. Obviously, in cases of indirect comparison, it may be easier to prove that the advertising does not constitute comparative advertising, since the implied reference to a competitor, or to his goods, services must be clear enough for a standard (well-informed) consumer and there is more room for interpretation for the courts in such types of cases. Thus, the understanding of the respective target group of the advertising shall be taken into consideration.

1.2.1. Direct identification

A competitor is recognisable directly if it is in particular mentioned in the comparison or figuratively represented.

1.2.1. Indirect identification

To be covered by the scope of the definition, it is also sufficient, if the competitor can be recognised indirectly. Reference can be made even indirectly, by implication or insinuation. The ECJ held that in order for there to be comparative advertising within the meaning of Article 2a. of Directive, it is sufficient for a representation to be made in any form which refers, even by implication, to a competitor or to the goods or services which he offers.

Indirect identification can be recognised on the basis of:

42 Howard Johnson: New EU directive on comparative advertising Tolley’s Communications Law Vol 3 Number 2 1998. 66. p
43 In an Austrian comparative TV advertisements advertiser shows the entrance of the building, where was the set of its competitor. (Hartlauer Case C-44/01, see it detailed way in World Trademark Law Report, 19 of June, 2003., or in article of Sándor Vida on comparative advertisements.)
44 C-112/99, Toshiba, para 31.
(i) reference to the advertisement of the competitor,
(ii) reference to business circumstances of the competitor,
(iii) direct or indirect group designations, or
(iv) situation on the relevant market. (Lastly mentioned method is heavily argued, see 2.6.) In certain Member States an advertisement claiming superiority was deemed to include a reference to identifiable competitor(s), as the number of the advertiser’s competitors on the relevant market was very small and could easily be managed.

2. Comparison

As this study mentioned earlier the most classical types of comparative advertising, when comparison of the advertiser and its competitors, or comparison of their products is the main element of the advertising activity. Also clear that some comparisons can not be regarded as comparative advertisements. The definition of comparative advertising clearly does not include comparisons of an advertiser’s own products. For example an advertiser promotes a dishwasher detergent by using the phrase “one hundred per cent more washing power”. This phrase means that new material is two times effective, than advertiser’s earlier product. The mentioned advertisements compares advertiser’s own products from quality point of view. Price comparisons are also frequently used. Advertisements states that the actual price of advertiser’s product is smaller than the earlier price was. This comparison does not refer to an identifiable competitor or its product. This type of comparison is outside the definition of comparative advertising. These special kinds of – quality or price – comparisons are regulated by advertising related rules of the unfair competition law, which means that they were allowed if they were not misleading. As one can recognise there are clear cases, when relatively easy to decide whether a comparison can or can not be regarded as comparative advertisements. However new types of comparison have arise, and borders sometimes are less clear.

2.1. ‘Abstract’ comparison

The so called ‘abstract’ comparison does not refer to an identifiable competitor or product. Without - explicit or implicit - identification of the competitor or its goods or services, in a case of abstract comparison there is no possibility to speak about comparative advertising.

2.2. System comparison

The so called ‘system comparison’ aims at demonstrating the merits of different means of distribution, production, application or functioning of products or services (for example, the comparison between the system “tampon” versus the system “sanitary towel”). Without - explicit or implicit - identification of the competitor or its goods or services, in a case of system comparison there is no possibility to speak about comparative advertising.

2.3. ‘Plural’ advertisements

This situation is opposite than cases in ‘abstract’ or system comparison. In this case we can find identified persons and/or products. The problem is that there are more than one person as competitors and/or more than one product as competitors’ goods or services. This is in my

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45 As such, in Austria. Further, if an undertaking has a dominant position in the market, Belgian jurisprudence considers the comparative advertising as a comparison with such dominant undertaking.
46 This is the so-called “instead of” price comparisons. The classic pattern is to say “instead of” and cross out a higher price.
47 Under Austrian law abstract comparison is outside the scope of the definition of comparative advertisements.
48 System comparison are considered by Austrian court pratice as abstract comparative advertising because the system comparisons usually do not refer to an identifiable competitor or product.
terminology the ‘plural’ advertisements. Have not decided yet whether a comparison with non one competitor, but more competitors can be qualified as a comparative advertising. An advertisements can establish a link between the advertiser and more competitor, or goods or services offered by the advertiser and more competitor. Question weather this ‘plural’ advertisements belongs to the comparative advertising or this is something else.

We can find two – different – answers: one derived from the text of the definition and one from the aim of European legislator.

Pursuant to Article 2a. of the Directive, ‘comparative advertising means any advertising which explicitly or by implication identifies a competitor, or goods or services offered by a competitor.’ The text mentions only one competitor (directly or through its goods or services). Having regard only the text, the answer: the ‘plural’ advertisements can not be qualified as a comparative advertising. What does it mean? Requirements for comparative advertising are irrelevant for ‘plural’ advertisements. In my opinion this is a bad result.

Having regard the function of the EC regulation I would prefer an other answered: the ‘plural’ advertisements belongs to the comparative advertising. Add to the aim of the regulation, the strengthen of the insider market (as you have seen in I. 3.), we can mention Recital (6) of the Directive 97/55 sets forth that it is desirable to provide a broad concept of comparative advertising in order to cover all types of comparative advertising.

The larger interpretation looks like – in my opinion – correct, and more useful, than the narrower. Consequence of this larger interpretation, that advertiser has to follow requirements for comparative advertising regulated in national laws on the base of Directive 97/55. In other case comparison is not permissible.

2.4. Non-commercial comparison

Comparative advertising is a market behaviour. Necessity of its special regulation, as you have seen in 5.1., based on market-related reasons. In the practice exist comparisons without commercial purposes. (Best examples see in 2.5.) Only the comparison made for commercial purposes falls under the scope of comparative advertising. Consequently, comparisons (tests) made by third parties (i.e., consumer organisations) to provide information to the public does not constitute a comparative advertisement provided it does not promote any goods or services.

2.5. Comparison made by third parties

Comparisons can be divided (i) comparisons made by competitors and (ii) comparison tests prepared by third parties who are not competitors. In many countries, product testing is done by consumer organisations and/or private or public institutions like the press, television and other media. It shall be examined as to whether the results of their testing may be used in advertising.

2.5.1 Test comparisons

It is generally permitted in Member States to carry out test comparisons and to publish the results. There are no legal restrictions on third parties carrying out test comparisons on products. Similarly, there are no restrictions on publishing correct test results.

49 Under Swiss law, comparative advertising may refer to an indeterminate number of competitors. Pursuant to UK case law, regarding implied references to a competitor, case law suggests that where an expression is such that it can only be construed as referring to one competitor, that is likely to amount to identifying that one competitor.

50 Generally, it is not allowed to publish product tests which are not true and therefore appropriate to mislead the public. Publication is appropriate, provided that publication would not result in the breach of some other legal obligation or liability, e.g. breach of copyright, breach of confidentiality, etc.
In my opinion test comparisons can not be regarded as comparative advertising. Only the comparison made for commercial purposes falls under the scope of comparative advertising. Organisations (which are not related to the advertiser or a competitor) preparing tests usually do not act intentionally with the objective to promote the sales and business of an undertaking.

2.5.2 The use of test result in comparative advertising

Results of test comparisons can be used during advertising activity. Generally permitted to make reference to test results in comparative advertising. For the use of the test in the advertising, in the majority of the countries, it is generally required to obtain the consent of the person/organisation who carried out the test.

If the advertiser refers to such comparative test, he shall be held liable for complying with the rules of comparative advertising.

2.6. Advertisements claiming superiority

2.6.1. Theoretical approach

Certain advertisements claim the superiority or uniqueness of the product, like "the best" and use of other superlatives. Including implicit comparison may well pose problems for advertisers using general statements such as "better than all the rest" etc. Famous slogans such as "nothing acts faster than Anadin" may well have to be used with more discretion.

What are legal consequences of this advertising? Two opinions are possible:
(i) This kind of behaviour involves - without indicating any specific competitor - per se a comparison with all other products of the same nature available on the market.
(ii) This kind of behaviour does not involve a comparison.

It can be concluded that the admissibility of advertisements claiming superiority can be subject either to specific rules on comparative advertising (i) or to general rules, i.e., prohibition of misleading (ii).

2.6.2. Comparative approach

There is certain divergence among the jurisdictions of Member States as to whether advertisements claiming superiority or uniqueness of the product fall under the scope of comparative advertising, or such advertisements are subject to general rules, i.e., the prohibition of misleading advertising.

(i) In the UK, such advertisements constitute a form of comparative advertising. In the Netherlands such advertisements may constitute a form of comparative advertising if the public will interpret the advertisement as a reference to one or more specific competitors

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51 In Switzerland test comparisons are allowed to the same extent as comparative advertising is admissible. The Swiss statutory law does not contain a definition of comparative advertising, and the jurisdiction limited itself to a very superficial attempt at defining it: comparative advertising refers to competitors. Thus, the notion of comparative advertising is construed broadly, and entails - contrary to EU law - comparative tests made by third parties.
52 The Austrian Supreme Court has ruled that the publication of a test result by a consumer protection organization was not an act of competition because there were no competitive interests.
53 However, Belgian law prohibits the reference to comparative test if such test was carried out by consumers' organization.
54 There are different reasons for the need of such consent: (i) copyright law (Germany, The Netherlands), (ii) database law protection on the test results (The Netherlands), (iii) special statutory provision of advertising law requiring such consent (Hungary).
55 Howard Johnson: New EU directive on comparative advertising
Tolley’s Communications Law Vol 3 Number 2 1998. 66. p
rather than every other competitor in the market. In Italy, using superlatives in the advertising is considered as a kind of indirect comparison with all market participants in the specific field of goods/services.\(^{56}\)

(ii) In contrast, in other countries (Austria, Belgium, France, Germany, Hungary, Spain) advertisements claiming superiority or uniqueness of the product - which do not include a reference to an identifiable competitor - are considered to be outside the definition of comparative advertising, and they are subject to general rules.\(^{57}\) However I have to add, that in Austria, an advertisement claiming superiority or uniqueness of the product - which do not include a reference to identifiable competitor(s), as the number of the advertiser’s competitors on the relevant market was very small and could easily be managed. Further, if an undertaking has a dominant position in the market, Belgian jurisprudence considers the comparative advertising as a comparison with such dominant undertaking.

2.6.3. My own understanding

In my opinion the situation is not so difficult as one can suppose at first sight. The difference is not larger than some legislation states that even such advertisements identifies the competitors, others states that identification is not automatical. It is clear, that identification, if we can speak about identification, happens in indirect way. As you can see the second solution (Austria, Belgium), differs from the first one (UK, the Nederlands), because the qualification is not automatic. They can imagine easier that advertisements claim the superiority or uniqueness of the product does not contains identification.

It seems to be desirable to apply the specific rules on comparative advertising if it can be identified with which competitor the comparison is made and such specific competitor can be regarded as the injured party.

On this base I suggest following the main rule in Divination given by the Directive. Identification of competitors or its product is important element of comparative advertising. In my opinion it not possible to decide generally whether advertisements claim the superiority or uniqueness of the product is qualified as a comparative advertising or not. Case by case have to control whether the questioned advertising contains identification or not. As far as interpretation of identification court practices of Member States are fare from each other.\(^{58}\)

2.7. Comparative advertising without comparison

In order for there to be comparative advertising within the meaning of Article 2a. of Directive, it is sufficient for a representation to be made in any form which refers, even by implication, to a competitor or to the goods or services which he offers. Therefore, if the competing products are merely referred to within the advertising, it in itself constitutes an instance of comparative advertising and it is irrelevant whether an actual comparison is made between the goods and services offered by the advertiser and those of a competitor.\(^{59}\)

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\(^{56}\) Under Swiss law advertising exaggeration, i.e. obtrusive praise that does not make sense, that is recognizable as such and therefore not taken seriously by the public, and obtrusive exaggeration or advertising resorting to value judgment do not fall within the ambit of the rules of comparative advertising. They may however be unlawful if they amount to unnecessary disparagement. This and other national examples were mentioned at LIDC Congress held in Budapest, 2004.

\(^{57}\) In particular, they must not be misleading and aggressive tendencies should be avoided as well as global disparagements.

\(^{58}\) The rules on comparative advertising will indeed apply to advertisements claiming superiority or uniqueness if there are only very few competitors and it is clear who is affected by a statement. For example, the Austrian Supreme Court came to this conclusion in a case where the advertiser of a newspaper claimed to be “faster and more current” and there was only one competing newspaper in the relevant market. On the other hand, in France, the use of the slogan “No. 1 of newspaper advertisements” was not considered as a comparative advertisement since the slogan did not refer, directly or indirectly, to any competitor newspaper. However, the slogan was considered to be unfair.

\(^{59}\) C-112/99, Toshiba, para 31
In my opinion the name 'comparative advertising' has some misleading nature. There are two kinds of interpretation of the comparative advertising: a narrower and a larger one.

(i) The narrower interpretation of this term is based on a real comparison. Historically this type of interpretation is older. Its original version covered comparison between only products. Even in a book, which was published in 1993, we can meet with such a narrower meaning: 'For instance, until recently the Austrian courts ruled invalid all form of comparative advertising (that is advertising which states that the advertised product is better than another named product)(36 p)...Comparative advertising (whereby one product is compared favourably to another named product) general is illegal in Germany (97 p) ...Comparative advertising (stating that the advertised brand is better than other named products) was banned for several years in Austria until the European Court of Human Rights ruled that commercial speech is entitled to some protection (287 p).

Similarly in Hungarian legal literature Katalin Mezey states that 'the central idea of comparative advertising is that quality or other important feature of a product or service is compared with an other product by way of identification of the other product or firm. I am not sure whether this ‘closely interpreted narrower’ definition covers or not services and comparison between competitors. Nowadays looks like clear, that it is comparative advertising, if two competitors, two products and/or two services are compared by the advertisements. Perhaps the original version of definition can be interpreted analogous way, or the definition has changed, its scope of application became a bit larger.

(ii) The wider interpretation of the term ‘comparative advertising’ covers other – not comparative – behaviours, too. This is something brand new. I am sure that is more than interpretation question. This result, such a wide interpretation can not be reached by way of interpretation. There is a new definition which was created by the Directive.

2.8. Conclusions on definition

There are several kinds of “comparisons” that are deemed outside the definition of comparative advertising, and at the same time there are comparative advertising without comparisons. Boarders are not clear enough. There is a real danger that court practices interpret different ways these boarders in Member States. This risk is against insider market concept. It would be useful to draw borderlines by a new Directive.

My feeling is, that there is a divergence between the definition of comparative advertising and its criteria. Some requirements are very clear way related to traditional comparisons, some other criteria’s scope of application is border: covers not only comparisons. Would be useful to thinking on it.

3. Hungarian interpretation of the phrase ‘comparative advertising’

3.1. Definition

The definition /Sec. 2 o of the Act/ on comparative advertising, though not a literal translation, is in conformity with the definition in Art. 3 (a) of the Directive, namely: “Comparative advertising: advertising that directly or indirectly allows the recognition of another enterprise which engages in the same or a similar activity as the advertiser, or of goods manufactures, sold or introduced by such other enterprise for the same or similar purpose as those featuring in the advertising.”

Though the wording of the Act is not literally identical (e.g. the terms “discredit” and “denigrate” do not figure in it) the subject matter of the quoted provisions is identical to that of the Directive.

### 3.1.1. Identification

The Act does not provide a distinction on direct or indirect comparative advertisements. As a result, there is no difference between direct or indirect comparative advertisement.\(^{62}\)

### 3.2. Hungarian solutions on uncertain problems of comparison

#### 3.2.1. Abstract comparison

The Hungarian legal practice makes a difference between a comparative advertisement and an advertisement containing a comparison (where no competitor can be identified). Hungarian legal literature (scholarly opinion)\(^{63}\) makes a distinction between so-called polarised and unpolarized advertising on the basis of the circumstance that in the former specific competitor(s) are identifiable, while in the later the comparison generally refers to the competing products available on the market.

#### 3.2.2. Fictious comparison

Hungarian advertising law specifies that it is forbidden to make any advertisement public, purporting or alluding a true option, that contains a comparison with a fictitious product or undertaking, with a product that is not available on the market, with a product or undertaking that cannot be clearly identified, or with a product or undertaking not of similar nature.\(^{64}\) Before the prohibition came into force there were precedents of fictitious comparisons in Hungarian case law. The power of a certain new washing powder was compared to cleaning capacity of so called ‘traditional’ washing powders. This method was relatively frequently used in the area of tooth-paste advertising. Today it is illegal. A possible result of the legal prohibition growing of tension between competitors, because comparison must be done with a concrete competitor or its concrete product.\(^{65}\)

#### 3.2.4. ‘Plural’ advertising

Though even the Hungarian definition of comparative advertising mention one competitor or one competitor’s products, we can not find such opinion that comparison with more competitors or more competitors’ products is outside of the scope of comparative advertising.\(^{66}\)

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\(^{62}\) Some examples from the Hungarian legal practice on advertising: Copies having lower quality than the original / LEGO bricks advertised as “compatibles” (Supreme Court, BH 1995/7/394). In the procedures CILLIT Cream (Metropolitan Court No. 2.K.30 624/2003) and CIF CREAM (Competition Council, No. 156/2002) comparative advertisements relating to liquid souring products were engaged as a result of a “war of advertisements” between owners of the two products. The distributor of the CILLIT product was condemned for lack of sufficient information in the TV advertisements, since he simply stated the superiority of his product, but the properties of the product were fully explained only in the instructions for use. The distributor of the CIF product was condemned for stating in TV advertisements that his product is better then CILLIT, as the latter harms objects in the kitchen and the bathroom. In the SENSATIONALE case, prices of imitating products (perfumes) were compared to those of famous branded products, without informing the consumers on the inferior quality of the former (Supreme Court, VFÉ 1995, 82). In the SENSATIONALE case the courts indirectly protected the reputed mark CHANEL too, not only the consumers.

\(^{63}\) Author is Kinga Pázmándi in Competition law audited by Tamás Sárközy, HVGOOrac Lap- és Könnykiadó, Budapest 2001. 517 p

\(^{64}\) Sec. 7/C of Act LVIII of 1997 on economic advertising activity

\(^{65}\) Pribula 93 p

\(^{66}\) As I have mentioned in 3.2.1. connected to so-called polarized and unpolarized advertising ‘specific competitor(s) are
3.2.5. Comparison made by third parties

Product testing is done by consumer organisations and/or private or public institutions are less frequently used in Hungary. There are no legal restrictions on third parties carrying out test comparisons on products. Similarly, there are no restrictions on publishing of these tests. This kind of activity is outside of advertising.

The results of the testing can be used in advertising. The commercial aim makes the difference between publishing tests and advertising using test results. Advertiser tries to get new markets with using results made by third parties. Comparison by a market-interested person using the objective test can be qualified as a comparative advertising.

3.2.6. Advertisements claiming superiority

Courts and the Competition Council penalized advertisings like ‘the best’67, or advertised a product as ‘No. 1.’68, a service as ‘most punctual and quickest’, the price as ‘unbeatable’ or cheapest etc. until now by referring to the general rules of misleading advertising.69 Sometimes similar behaviour is qualified as misleading comparative advertising. Advertiser has the right (this is its obligation, too) to evidence statements of its advertisements claiming superiority. Scientific institutions are relatively frequently asked in such questions. On the base of Hungarian court practice I can state, that evidencing are most of the cases unsuccessful when advertisements used „most …” phrase.70 In the procedure HEAD & SHOULDERS71 shampoos against dandruff were compared using the terms “the best, the most effective shampoo against dandruff”. An interpretation relating to the goods was not necessary in any of the quoted cases.72

III. The concept of the EU Commission’s Proposed Directive on the misleading nature of an advertisement

On June 18, 2003, the EU Commission presented a Proposal for a Directive concerning unfair business-to-consumer commercial practices in the Internal Market and amending directives 84/450/EEC, 97/7/EC and 98/27/EC (the Unfair Commercial Practices Directive)73 (hereinafter: the “Proposed Directive”). Recital (5) of this Proposed Directive indicates that it approximates the laws of the Member States on unfair commercial practices (including unfair advertising) which harm consumers’ economic interests. In line with this, the Proposed Directive sets forth that it neither covers nor affects the national laws on unfair commercial practices which harm only competitors’ economic interests or which relate to a transaction between traders. Further, it does not address the provisions of Directive 84/450/EEC on advertising (including comparative advertising) which is misleading to businesses, but not misleading for consumers.

67 DANONE kefir was advertised as “the best” - Metropolitan Court, VFÉ 1996, 354;
68 DREHER beer was advertised as “No. 1.” - Competition Council, VFÉ 1995, 194
69 Considered as an advertisement containing a comparison, the competition authority found the slogan ‘it removes easily the stain and scale which other products leave’ misleading because the product – according to the instruction of use - could not be used on all surfaces in the bathroom and kitchen.
70 The ‘most …’ phrase means generally more than evidenced by advertiser. F.e. Vj-217/2000
71 Competition Council, No. 4/2003
72 The referred cases are available on the Home page of the Competition Office under www.gvh.hu.hu.
Pursuant to Article 14 (4) of the Proposed Directive, Article 3a of the Directive shall be replaced by a partially new list of conditions which each instance of comparative advertisement shall comply with. The Commission’s rational for the new proposal states that, for the sake of clarity and simplicity, the Proposed Directive incorporates the misleading advertising directive’s B2C provisions (i.e., provisions dealing with advertising reaching or directed at consumers) and limits the scope of the existing Directive to business-to-business advertising (i.e., provisions dealing with advertising reaching or directed at businesses) and comparative advertising which may harm a competitor (by denigration, for example) but where there is no consumer detriment (page 8). Thus, as a result of the amendment, subsections (a) and (d) will be deleted from the Directive.

I do not agree with the concept. I would like mention three reasons.

(i) One cannot separate exactly the aspects of harm to consumer and harm to competitor. Therefore, application of the Directive will difficult in the practice.

(ii) For the purposes of the Proposed Directive, in compliance with the civil law definition in EU legislation, consumer means any natural person who, in commercial practices (covered by the Proposed Directive), is acting for purposes which are outside his trade, business or profession. In Hungary the concept of consumer in competition law is not restricted to natural persons. Therefore in Hungary we have to count with special extra problems.

(iii) Solution of the Proposed Directive misleadingly suggests that only two kinds of interest exist, i.e. interest of consumers and interest of competitors. A general policy issue is whether comparative advertising should be allowed or prohibited, this involves a balancing of various interests. On the one hand, such advertising would enhance consumer knowledge, but on the other we may not wish companies to gain a free ride on the back of someone else’s success. The political balance must be struck between the interests of brand owners and the interests of the market economy. In 3.2. point we showed, that the law has to protect even rightholders’ interest. They are similarly harmed by comparative advertising as consumers. Proposed Directive forgets protecting interest of this group of persons. Perhaps European legislator though that the original Directive’s task to protect both competitors both rightholders. In my opinion this two kinds of interest can not be protected on the same way. Interests of righolders are closer to interest of consumers, than to interests of competitors, even that these two positions sometimes belong to one person.

Summary

This study tried to show the economic function of the comparative advertising, its risks, interests to be protected and the main features of its regulation.

The main part was about the definition of comparative advertising. In legal literature the requirements of comparative advertising is the most important problem, the definition of comparative advertising looks like a second range question. This topic generally is missing from books and articles. In my opinion it is important to determine the comparative advertising firstly because only this type of comparison can be regarded as lawful in certain circumstances, secondly because in this case legal requirements must been followed. All the EU countries have implemented the Directive in their legal systems, with essentially identical requirements set forth in the Directive. As far as the definitions of the comparative advertising is concerned, the situation less homogeneous. It was the main reason to do some researches on this topic.

In my opinion the name ‘comparative advertising’ has some misleading nature. Theoretically there are two kinds of interpretation of the comparative advertising: a narrower and a larger one. The

narrower interpretation of this term is based on a real comparison. Two competitors, two products and/or two services are compared by the advertisements. The larger interpretation of the term ‘comparative advertising’ covers other – not comparative – behaviours, too. Identification of a person with high reputation, or a famous product, a well-known service, a registered trademark, or trade name must be qualified as a comparative advertising on the base of the definition given by the Directive. In this study I have tried to draw the attention to a change. Definition of comparative advertising has changed. This change has happened in the legislation and – partly – in the court practice, but the original definition is living in our mentality. Our first reaction on comparative advertising is the same as decades ago was. Picture of comparative advertising emerging in our ideas is a picture of comparison. It is not totally bad, because most of comparative advertisements contain comparisons. But our first idea wrong, because comparative advertising is more than comparison, in certain cases comparative advertising exists even without comparison. Even an advertising without direct comparison can be harmful if it exploits the renown of an other person or other persons.

Definition became wider by EC legislation. A larger circle of situations accepted as comparative advertising by the court practice of Member States. Comparisons between more than two competitors or their products, using test results made by third parties in advertisements are good examples.

This process created some uncertainty. Whether abstract comparison, system comparison, fictious comparison can be or must be qualified as comparative advertising? If the answere is ‘yes’, whether legal criteria must be the same in these cases, or we need new requirements? How the advertisements claiming superiority can qualified?

For answering these questions important to analyse difference between requirements for comparative advertising and requirement for advertising in general.

(i) If the legal system is able to protect all of attached persons’ interests using traditional rules connected to the misleading advertising or more generally connected to unfair competition, we need not create new categories, and new rules.

(ii) But if traditional legal tools are not efficient enough, can be usefull widening the definition of comparative advertising. In this way legal praxis gets possibility to use special tools against certain advertisers.

(iii) Legal praxis usually tries to apply existing legal tools to solve new problems. Sometimes it is impossible, new criteria, new prohibitions must be created.

This study showed a lot of examples what kind of answeres are given by EC and Member States, how they try to solve their new problems. Chosen solutions by Member States are different from each other. Existing situation is contrary to the original aim of EC. For ensuring a real inside market would be useful to find one answere, or similar solutions. Instead of this, Commission is thinking on a new, consumer-protection oriented, additional legislation. There is no real reason why has the consumer oriented legislation become stonger, than the interpretation based on the free movement of goods and services. Application of planned rules will be difficoult. Higher level uncertainty and more diffused court practice will be the result of the planned new Directive.

I hope legal answeres become clear in a certain period. We have a lot to do for this. We have to analyse how different methods are used in Member States, which solution is the most efficient. Using the so called ‘best prectice’ technic, EC is able to help Member States to introduce the most efficient method into their legislation.
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THE AGRICULTURAL COMPETITION LAW OF HUNGARY

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Field of research: Agrarian Law

This lecture was inspired by the European Agricultural Law Association, particularly by Dr. Wolfgang Winkler, who is a professor of the University of Göttingen, and an expert in European Agricultural Law. In May 2003 our professor, Dr. Tamás Prugberger was called upon to prepare the country report on the situation of the Hungarian Agricultural Competition Law for the next session of the European Agricultural Law Association. He then gave us this noble task. The study was completed by September 2003 but it has not been published yet.

A. National Competition Law
I. Legal foundation of national Competition Law (1)

1. Which legal basis has your legislation for Competition Law?
- In respect to practices concerning the trade between the European Communities and Hungary the governing law is basically the competition law of the Communities on the basis of the European Agreement promulgated by the Act I of 1994.
- In other cases the Hungarian domestic regulation is principally governing. The Act LVII of 1996 on the Prohibition of Unfair and Restrictive Market Practices (hereinafter Tptv.) serves as a basis for the natural competition law and every single additional government decree of block exemption and certain parts of the Act LVIII of 1997 on Business Advertising Activity are linked with it.

We have to point out that our domestic regulation is about to entirely comply with the EU requirements. During its preparation certain considerations of the EU drawn up by the Treaty of Rome (See Articles 81 and 82), by the EC regulations on block exemption from the vertical cartel and by EC directive on the misleading advertising activity have been taken into account, as well as viewpoints formulated by the case-law of the European Comission and the European Court of Justice (e.g.: Woodpulp, Dyestuffs, ICI, United Brands, Hoffmann-La Roche, Sea Containers, Continental Can, Nestle/Perrier cases).
- Comparing our regulation with the EU competition law the main difference (i.e. a difference which is still not contrary to the EU law ) lies in the material scope. That is to say the Hungarian Act of Competition is essentially sector neutral. While in the competition law of the EU special rules apply to the coal-and steel products, the agriculture and the transport, in the Hungarian Competition Act do not exist such sectorial distinction. The other field of differences resulting from the material scope is of the practices regulated therein. Namely besides the anti-trust law, the prohibition of the abuse of a dominant position and the control of mergers the scope of the Hungarian Competition law applies also to rules prohibiting the unfair competition and protecting
the consumers’ interest. At the same time the Hungarian regulation (opposite to the Union norms) does not contain any rules either concerning the role of the state in the competition law or about the position of public undertakings (i.e.: undertakings which perform public duties).

2. Which instruments exist in your legislation for the control of restrictions on competition: Principle of prohibition and/or principle of malpractice (state controlled intervention against improper restraint of competition)?

The principles set forth below are used in connection with the provisions of cartels in the Hungarian competition law. These principles do not apply to the two other fields of the law of the restriction of competition in a broader meaning, i.e. to the abuse of a dominant position and to the merger. This little remark may help during the interpretation of this report.

What does the principle of prohibition and/or malpractice mean in terms of the Hungarian Competition Law, more explicitly in relation to the cartel rules?

Principle of prohibition: upon this principle - after having established the natural exceptions - cartel qualifies as prohibited automatically. In the Member States of the Union that principle is mainly enforced at the moment.

Principle of malpractice: this principle does not prohibit the cartel itself, but the abusive practice thereof, by which the competition will be damaged.

Almost every legislation following the latter principle generally require the registration of the cartels, i.e. the 1) voluntary notification and the 2) registration.

Based on the principle of prohibition the Hungarian Competition law extensively regulates that which shall qualify as a cartel and also prohibits it universally.

Tptv. Section 11, Subsections (1)-(2):

(1) Agreements between undertakings and co-ordinated practices, as well as the decisions of the social organisations of undertakings, public corporations, unions and other similar organisations of undertakings, unions (hereinafter collectively “agreements”), which are aimed at the prevention, restriction or distortion of economic competition, or which may display or do display such an effect, are prohibited. An agreement concluded between undertakings that are not unrelated shall not be construed as such.

(2) This prohibition shall in particular apply to the following:

a) fixing the purchase or sales prices, and defining other business conditions directly or indirectly;
b) restricting or keeping manufacture, distribution, technical development or investment under control;
c) dividing the sources of purchases and restricting the freedom of choosing from among them, as well as excluding a set circle of consumers from the purchase of certain goods;
d) dividing the market, excluding anybody from selling, and restricting the choice of sales opportunities;
e) collusion between competitors in connection with a bidding process;
f) preventing anybody from entering the market;
g) the case where, in respect of transactions to an identical value or of the same nature, certain partners are discriminated against, including the use of prices, payment deadlines, discriminatory sales or purchase conditions or the employment of methods which cause disadvantage to certain business partners in the competition;
h) rendering the conclusion of a contract dependent upon the assumption of obligations which, due to their nature or with regard to the usual contractual practice, do not form part of the subject of the contract.

– Does your legislation contain provision for notifying or registering restraints of competition? – Please indicate the cases, relevant for the agro-business, in which the principle of prohibition
respectively the principle of prohibition respectively the principle of malpractice is applicable and which restrains of competition have to be notified or registered.

The Hungarian cartel law, as such does not contain these legal institutions, however they can be found in the law of the restriction of competition used in a broader meaning. Namely there is a compulsory authorisation by the merger, as well as a notification required in the cartel law.

1. Merger (concentration of companies): \textit{Tptv.} Section 24 Subsection (1) (See more: Section 23, Subsections (1)-(3), Section 14, Subsections (1)-(2.))

2. Concern law (Act on the Business Associations)

3. Which sanctions are provided for illegal restrains of competition and malpractice (ban for restraint of competition; instructions for price regulation by governmental agency? Imposed fine by governmental agency; penal sanctions? Invalidity of restraint of competitions; compensations and/or injunctive relief by private persons or associations?

Legal consequences of cartel are laid down by two acts: \textit{Ptk.} (Civil Code) and the \textit{Tptv.}

3.1. Nullity: its critera are stipulated in the Civil Code. This a typical civil law consequence.

3.2. Legal consequences of the prohibition of cartel are established in resolutions adopted by the Office of Economic Competition (as a budgetary agency). The Office
- may declare a conduct illegal,
- may order the termination of any illegal conduct,
- may prohibit the continuation of any illegal conduct,
- may impose a fine for any violation of the provisions and/or
- may prescribe certain obligations in connection with illegal conduct.

4. Does your legislation differentiate between horizontal and vertical restrains if competition?

Yes, it does. The \textit{Tptv.} (the Hungarian Competition Act) has introduced a general anti-trust provision, which also applies to the vertical cartels, while in the system of block exemptions the vertical cartels are exempted from the scope of the anti-trust law.

5. Are there any exceptions or exemptions to illegality of horizontal and vertical restrains of competition?

As it can be seen above there are exceptions and circumstances of exemption. Exceptions can be classified into three groups:

\textit{I. Exceptions conferred by law:}
- bagatell cartel (\textit{Tptv.} Sections 13-14),
- an agreement concluded between undertakings that are not unrelated (\textit{Tptv.} Section 11, Subsection (1), last sentence, Section 15, Subsection (1)).


\textit{III. Exemption upon an individual application} by the Office of Economic Competition (\textit{Tptv.} Sections 17-20.)

6. Are there any rules concerning recommendations (e.g. price recommendations)?

Act LXXXVII of 1990 on Pricing (see Section 1, Subsection (2))

\textsuperscript{1} Similar to the Question I.2. the answer is confined to the cartel.
Act LVIII of 1997 on Business Advertising Activity
Decrees of Block Exemption (see listed under question 5)
Act CXLIV of 1997 on Business Associations
Act XVI of 2003 on Agricultural Market Rules
Act CII of 1994 on Local Appellation Council
Decrees of Subvention (e.g.:No. 26/2003.(III.11.) of the Minister of Agriculture)

7. Are there special provisions concerning abuse of dominant market position?

Yes, there are. See the following provisions of the Competition Act (Tptv. Chapter V.: Prohibition of Abuse of Dominant Position)

It is prohibited to abuse dominant position, in particular:

a) to establish purchase or sales prices unfairly in business relations, including the case of the use of general contractual conditions, or to stipulate unjustified advantages in another manner, or to force the acceptance of disadvantageous terms and conditions on another party;

b) to restrict production, distribution or technical development to the detriment of the consumers;

c) to refuse to establish or maintain business relations adequate for the nature of the transaction without any justification;

d) to influence the other party's economic decisions for the purpose of gaining unjustified advantages;

e) to withdraw goods from general circulation or to withhold goods without justification prior to price rises or for the purpose of causing prices to rise, or in a way otherwise capable of securing unjustified advantages or causing a disadvantage in competition;

f) to render the supply and acceptance of goods dependent upon the supply or acceptance of other goods, or to render the conclusion of a contract dependent upon the assumption of obligations which, due to their nature, or with regard to the usual contractual practice, do not form part of the subject of the contract;

g) in the case of transactions to an identical value or of the same nature, to discriminate against certain business partners without justification, including the use of prices, payment deadlines, discriminatory sales or purchase conditions and the employment of methods which cause disadvantage to certain business partners in the competition;

h) to force competitors off the market concerned, or to use overly low prices based not upon greater efficiency compared with the competitors which are capable of preventing competitors from entering the market;

i) to hinder competitors from entering the market in any other unjustified manner; or

j) to create an undue disadvantageous market situation for the competitors or to influence their economic decisions for the purpose of gaining unjustified benefits.

Dominant position shall mean when an undertaking is in a position to conduct its economic activities in a given market in a manner largely independent of others, without having to consider the market behavior of its competitors, suppliers, buyers or other business partners in so far as to eliminate effective competition. The following shall, in particular, be examined in assessing dominant position:

a) the costs and risks entailed by entry into the market concerned and exit therefrom, and the realization of the technical, economic or legal conditions that it requires;

b) the assets, financial strength and revenue situation of the undertaking, and/or the development thereof;

c) the structure of the market concerned, the ratios of market shares, the conduct of the participants of the market, and the economic influence exercised by the undertaking over the development of the market.

A single undertaking or several undertakings together can be in a dominant position.

8. Are there any rules referring to discriminatory measures or obstructive competition practices?
Yes, there are plenty of these rules throughout the whole Competition Act. (In connection with the law of limitation of competition see answers under questions 2,7,9.)

9. Are there any rules concerning merges of companies (e.g. merges of co-operatives)?

Yes, there is. The whole chapter VI (Controlling the Interlocking of Undertakings) of Act LVII of 1997 (Tptv.) is concerned with this issue. 

Section 23 (1) Undertakings become interlocked (concentrated) if

a) two or more previously independent (unrelated) companies merge, or one merges into another, or a part of an undertaking becomes a part of another undertaking which is independent of the first undertaking,

b) where one or more undertakings acquire direct or indirect control of the whole or parts of one or more other, previously independent undertakings, or

c) several independent (unrelated) undertakings jointly set up an undertaking to be controlled by them in which they unite their identical or complementary activities pursued earlier, provided that this does not qualify as an agreement restricting competition as defined in Section 11.

(2) For the purposes of this Act, one or more undertakings acting jointly shall be deemed to have direct control if

a) it holds over fifty per cent of the shares, stocks or voting rights in the controlled undertaking, or

b) has the power to designate, appoint or dismiss the majority of the executive officers of the other undertaking, or

c) has the power, by contract, to assert major influence over the decisions of the other undertaking, or

d) acquires the ability to assert major influence over the decisions of the other undertaking.

(3) For the purposes of this Act, an undertaking shall be deemed to have indirect control over another undertaking when the latter is controlled, whether independently or jointly, by one or more undertakings under the control of the former.

(4) The activities of a liquidator or receiver shall not be considered as control.

(5) For the purposes of this Act, 'business unit' shall mean the assets or rights, including clients and customers, that, if acquired, enable the acquiring undertaking to enter a market by itself or together with the assets and rights at its disposal.

Section 24 (1) Authorization from the Office of Economic Competition shall be required for any interlocking directorates of undertakings if the combined net sales revenue of the undertakings involved (Section 26) in the previous financial year exceeded HUF ten (10) billion and

a) the previous year's net sales revenue of the business unit, the merging or the acquired undertaking or - in respect of fusion - of at least two of the undertakings directly involved [Subsection (2) of Section 26] - together with the indirect participants that are affiliated with the undertaking [Subsection (3) of Section 26] - is in excess of HUF five hundred (500) million, or

b) together with the previous year's net sales revenue of the business unit, calculated as per paragraph a) the merging or the acquired undertaking or of the directly involved undertakings with net sales revenue below HUF five hundred (500) million, the merging or acquiring undertaking or undertakings with interlocking directorates with net sales revenue in excess of HUF five hundred (500) million and their affiliated direct participants [Subsection (3) of Section 26] have established interlocking directorates with an undertaking within the two preceding years for a combined total of net sales revenue in excess of HUF five hundred (500) million.

(2) For credit institutions with interlocking directorates, ten (10) percent of the balance sheet total shall be taken into account instead of the net sales revenue. For insurance companies with interlocking directorates, the value of the secured (contracted) gross insurance premiums shall be taken into account instead of the net sales revenue. For investment firms and funds with interlocking directorates, the revenue from investment services and membership fees, respectively, shall be taken into account.
Section 25 The temporary (not to exceed one year) acquisition of control or assets by an insurance company, credit institution, financial holding company, mixed-activity holding company, investment firm or property management organization shall not be deemed interlocking directorates, if such acquisition is made in preparation of resale, and if control is not exercised, or it is limited to an extent that is absolutely necessary. The Office of Economic Competition may authorize the extension of said one-year period if the undertaking in question provides proof that alienation could not be accomplished within one year.

Section 26 (1) The undertakings concerned are the undertakings involved directly and indirectly in the interlocking.
(2) Direct participants are the ones between whom the interlocking takes place.
(3) Indirect participants are those
   a) who are controlled by a direct participant as defined in Subsection (2) or (3) of Section 23;
   b) who control a direct participant as defined in paragraph a);
   c) who are controlled by an indirect participant as defined in paragraph b), in addition to a direct participant, in accordance with paragraph a);
   d) who are controlled by two or more participants jointly, regardless of whether they are direct participants or indirect participants as listed in paragraphs a) to c).
(4) In the course of determining the circle of direct participants, those whose right of control expires as a result of the interlocking shall be disregarded.

Section 27 (1) For the purposes of Subsections (1) of Section 24, in the course of calculating the net sales revenues, the turnover between the undertakings concerned (Section 26) or between the parts thereof shall be disregarded.
(2) In the course of calculating the net sales revenues of (non-resident) undertakings whose corporate domicile is abroad, the net sales revenues generated in the previous business year from the goods sold in the territory of the Republic of Hungary shall be taken into account.
(3) In calculating the net sales revenues of the undertakings concerned, majority owned by the State or by local governments, that undertaking comprising an economic unit shall be taken into account which has an independent right of decision-making in respect of defining its market attitude.
(4) In respect of the alienation of business units, the net revenue received by the undertaking from the utilization of assets and rights shall be taken into consideration.

Section 28 (1) In the case of merger or fusion, the direct participant or, in all other cases, the party acquiring the business unit or direct control must - as prescribed under Section 24 - apply for authorization for interlocking directorates.
(2) The application for permission shall be submitted within thirty (30) days reckoned from the earliest of the following dates: the publication of the public invitation to tender, the conclusion of the contract or the acquisition of the right of control.
(3) In the case of the interlocking of credit institutions as well as of insurance companies, the application for permission shall be submitted to the Office of Economic Competition at the same date as the application for the permit of the supervisory agency defined in a separate legal rule.

Section 29 The permission of the Office of Economic Competition is required for the conclusion of a contract resulting in an interlocking as defined in Section 24.

Section 30 (1) When assessing an application for permission, the advantages and disadvantages resulting from the interlocking shall be assessed. In the course of this, the following shall be examined in particular:
   a) the structure of the markets concerned; the existing or potential competition, the purchase and sales opportunities on the markets concerned; the costs and risks, as well as the technical, economic and legal conditions, of entry into the market and exit therefrom; the expected effect of the interlocking upon the competition on the markets concerned;
   b) the market situation and strategy of the undertakings concerned, their economic and financial capability, their business attitude, their competitiveness on domestic and foreign markets, and any expected changes therein;
c) the effect of the interlocking upon the suppliers, the intermediate and final consumers.

(2) The Office of Economic Competition may not refuse to grant authorization if, with regard to the contents of Subsection (1), the interlocking directorates do not create or intensify dominant position in so far as to prevent the development, maintenance or expansion of effective competition in the given market (Section 14) or in a considerable fraction thereof.

(3) In the interest of reducing the disadvantageous effects of interlocking directorates, the Office of Economic Competition may make its authorization contingent upon prior or subsequent conditions; certain obligations, such as having to alienate certain business units or other assets within a prescribed deadline; or termination of control over an undertaking that is indirectly involved.

(4) If authorization is granted as contingent on any prior condition, it shall become operative once the condition has been satisfied. An authorization contingent on any subsequent condition shall become operative when it is granted; however, it shall be cancelled if the condition is not satisfied.

(5) The scope of authorization granted for interlocking directorates shall include the restrictive market practices necessary for carrying out such interlocking directorates.

Section 31 If, in the course of a competition control procedure, it is established that unauthorized interlocking directorates (which, according to Section 24, require authorization) could not have been authorized, the Office of Economic Competition, in order to restore effective competition, may prescribe the separation or alienation of the merged undertakings or assets and business units; termination of joint control; or some other obligation, and it shall set an appropriate deadline for doing so.

Section 32 (1) The Office of Economic Competition shall withdraw its decision passed on the basis of Section 30, if

a) granting of the permission in a decision not reviewed by the court is based upon the misleading communication of a fact important from the respect of making the decision, or

b) the obliged undertaking has failed to perform any of the obligations stipulated in the decision.

(2) The Office of Economic Competition may amend its decisions passed on the basis of Section 30 if the obligor has failed to perform any of the obligations or is unable to satisfy any of the conditions laid down in the decision for reasons beyond his control.

10. Are Competition Law based decisions of governmental agancies or courts solely focused on aspects of competitions, or do they equally account aspects of economic and social policy?

Decision-making bodies clearly put the emphasis on the aspects of competition.

1. Tptv. Section 17, Subsection (1)

Agreements or planned agreements shall be exempted from the prohibition declared by Article 11 on individual application by the decision of the Hungarian competition authority, provided that

a) they contribute to a more reasonable organisation of production or distribution, the promotion of technical or economic progress, or the improvement of competitiveness or of the protection of the environment;

b) they allow consumers a fair share of the resulting benefit;

c) the concomitant restriction or exclusion of competition does not exceed the extent necessary to attain economically justified common goals;

d) they do not create the possibility of excluding competition in respect of a substantial part of the products concerned.

2. Tptv. Section 22, Subsection (2)-(3)

The following shall, in particular, be examined in assessing dominant position:

a) the costs and risks entailed by entry into the market concerned and exit therefrom, and the realisation of the technical, economic or legal conditions that it requires;

b) the assets, financial strength and revenue situation of the undertaking, and/or the development thereof;
c) the structure of the market concerned, the ratios of market shares, the conduct of the participants of the market, and the economic influence exercised by the undertaking over the development of the market. A single undertaking or several undertakings together can be in an dominant position.

3. Tptv. Section 30, subsections (1)-(2).

When assessing an application for permission, the advantages and disadvantages resulting from the interlocking shall be assessed. In the course of this, the following shall be examined in particular:

a) the structure of the markets concerned; the existing or potential competition, the purchase and sales opportunities on the markets concerned; the costs and risks, as well as the technical, economic and legal conditions, of entry into the market and exit therefrom; the expected effect of the interlocking upon the competition on the markets concerned;

b) the market situation and strategy of the undertakings concerned, their economic and financial capability, their business attitude, their competitiveness on domestic and foreign markets, and any expected changes therein;

c) the effect of the interlocking upon the suppliers, the intermediate and final consumers.

The Office of Economic Competition may not refuse to grant authorization if, with regard to the contents of Subsection (1), the interlocking directorates do not create or intensify dominant position in so far as to prevent the development, maintenance or expansion of effective competition in the given market (Section 14) or in a considerable fraction thereof.

II. Special provisions for agriculture in Competition Law?

Pre remark: Competition Law has two possible functions in the agriculture sector. On the one hand Competition Law can broaden the possibilities of farmers comparison to commercial companies. On the other hand farmers can protected by the Competition Law in a special way.

1. Extension of farmers possibilities due to Competition Law?

1.1. Does your legislation contain special provisions for farmers or general provisions, which also farmers can invoke?

The relevant legal regulation for farmers determines only the framework of the production and does not contain any particular rules of competition since the scope of the Tptv. also applies to the agriculture. Particular rules of competition arrived at the Hungarian legal system as a result of the re-regulation of the Act on the agricultural market rules (Act XVI of 2003).

1.2. If yes, to which business and products are these special provisions applied?

Special rules apply to the viniculture, the activities of forestry, hunting and fishing. Though a few of these statutory instruments have competition law effects, they still not qualify as laws of competition.

1.3 Are there exceptions for horizontal restrains of competition in agro-sector?

In the Hungarian national law doesn’t contain special competition rules in agro-sector. The any exceptions we are mentioned in the A/1.5 point.

1.4. Does your legislation feature special provisions for co-operative producer organisations?
In respect to producers’ organisations (associations) particular rules are laid down in the *Act CXL* of 2000 on the new co-operatives. However, these rules are of corporate law nature rather than of competition law. In case of the dissolution without succession of co-operatives the association of co-operatives inherits the assets which can not be distributed, provided that there is no other co-operative whose objectives are corresponding to the educational, cultural and social objectives specified by the former co-operative.

### 1.5. Are there any special provisions for co-operatives in the forest sector?

Since 1994 one special association has operated in the Hungarian forestry sector, the so-called “forest management association”. This organisation integrates forest farmers whose land does not reach the 1500 square meter limit, therefore it is not suitable for an individual forest management. Should two-third of the proprietors initiate the foundation of such organisation on a given territory, the rest one-third automatically becomes the membership.

### 1.6. Are there exceptions for vertical restraints of competition in the agro-sector?

We are rather acquainted with horizontal limits of competition.

### 1.7. Does your legislation accept organisation for special branches of trade (Organisations of producing, processing and marketing business of same agricultural product) and if yes, which practical impact has such a declaration in your country?

There are such organisations, but their activity does not fall directly within the scope of the restriction of competition. Namely in the gardening sector and in other producing sectors the competent minister may recognise an organisation as a Marketing Organisation of Producers (Termelői Értékesítő Szervezet) or a Producers’ Group irrespective of their legal form. In the first year of their activity this is only a provisional recognition, but in case the income of such organisations reaches 150 million forints they are entitled to the permanent qualification. Up to 150 million forints 20 % of their actually confirmed income and additional 6% of their revenue above 150 million they receive as a state subsidy, which must be used for purchasing instruments needed for the cultivation.

### 1.8. Does your legislation know special provisions concerning leasing agreements for contacts in the area of plant breeding and seed?

We are not familiar with it.

### 1.9. Does your legislation feature the possibility of declaring horizontal or vertical restraints of competition by organisations and associations as generally binding? If yes, which practical impact has such a declaration your country?

Does not, since the principle of prohibition applies to cartels in Hungary. (See 1.12.)

### 1.10. Are there any restrictions on exemptions for the agro-sector by supervisory body combating the abuse of exemptions?

Does not.
2. Protection of farmers by Competition law

2.1. Does your legislation know special provisions protecting farmers from discriminatory or obstructive practices?

Concerning this question there are two provisions of the above mentioned Act XVI of 2003 on the agricultural market rules. One of them prohibits retail chains disposing of a dominant customer power to sale their products under purchase price. The other provision requires to perform payments to producers at least in 30 days after the receipt of goods. In the interest of the discipline of payment longer terms are prohibited.

2.2. If no, to what extent are farmers protected against discriminatory measures (e.g. concerning distribution of sugar quotas to producer companies) or obstructive practices (e.g. sale of agricultural products below purchase price) by the generally applicable provisions?

The main problem in Hungary lies in the situation that there has not been developed the practice nor the legal instruments according to which farmers shall to be provided with economical protection. Our Act on the agricultural market rules, which promises an EU-conform regulation, entered into force in 2003. According to this act the regulation of the product scales still remains in the hand of the Ministry of Agriculture and Rural Development and persons taking part in the production only have the right of the expression of opinion during the determination of their own market. It was the Office of Economic Competition itself who protested sharply the provisions of the agricultural market rules regulating the selling under prefixed purchase price.

In his view legal actions against the abuse of consumer's power will result in an unnecessary profiteering and is not an effective instrument for breaking down the dominant position of retailers’ chains.

In Hungary the sugar market did not fall within the scope of the directly regulated agricultural market which controls the strategical products, therefore acquisition at a guaranteed price and quota were not be enforced. Only on the milk market exists a quota in the Western European sense, but there has not been any corrupt practice during its distribution. Examples rather can be mentioned, in connection with such practices of acquisition companies having a dominant consumer's power, e.g. no performance for the delivered goods (Civil proceedings of MIZO Pécs Rt in 2001).

B. National Law an EC law

1. Which conflicts arose until now between EC law and your national legislation’s because of supremacy of Community Law (proceedings before the European Commission or the European Court Justice)?

In respect to the agrarian competition law I have not met a case where proceedings were brought against a resolution of the court or of the Office of Economic Competition.

2. Has your national legislation been modified due to EC Law or will modifications become necessary in the future?

In this regard an essential amendment is justified. The judicial harmonisation has now reached a certain level at which we are able to apply the relevant means of market of the Common Agricultural Policy. In this respect the Act XVI of 2003 on the agricultural market rules is regarded as only a provisional one, because after 2004 the provisions of the common market organisations will be directly effective. In relation to the competition law Hungary does not apply the clause included in the Treaty of Rome, which takes the competition rules of the agricultural sector out of the scope of the Common Trade Policy and the European Competition Law. It is not sure whether
The Agricultural Competition Law of Hungary

this article needs to be amended seeing that there has been an effort to approach the market rules of the Common Agricultural Policy to the Competition Law since 2000. As an exception to the competition rules the regulation concerning this area might remain, but there is a little chance for the harmonisation of this issue in Hungary.

C. Assessment of the effective Competition Law concerning agriculture

1. Are the operational possibilities under Competition Law of agricultural companies sufficient in order to establish agricultural co-operation and to realise vertical integration in agriculture respectively under special provisions for the agriculture?

1990 onwards the Hungarian agricultural policy has pushed into the background the historical interdependence between the chains of the big farms and the small farms constructed on big farms. The breaking up of this chain has led to a drastic decline of the Hungarian agricultural output. The buyer’s market has changed and other qualities are required. The property relations has moved towards the small enterprise, but most of the new owners’ sphere was not interested in the agricultural production. Therefore a dominant part of the production was left to the former co-operatives which have reorganised as trade associations for the sake of a better profit. Owing to the political rotation the agriculture has lost its economical power, and at the same time its policymaking importance, too. Thus the agricultural policies realised in the last third of the political cycle had focused on problems of less economical importance (e.g.: a arable land purchase, National Land Reserve and the problem of the so-called ‘pocket contracts’) As a result of the approximation of laws preferred agricultural associations have been set up which may assist the integration. The regulation of subvention referring to the above mentioned associations changes year by year and the granting is bound to a bureaucratic state recognition. Preferential loans, tax law and other legal instruments are not associated with it.

2. Is agriculture adequately protected by Competition Law or should these provisions be enlarged (e.g. sale below purchase price)?

Before widening the particular rules of competition in Hungary dividing lines should be clarified between agricultural and trade law activities. One should see the European expectation which requires the harmonisation of this area. Pursuant to commercial lawyers the disintegration of the uniform competition law would make this regulation incomprehensive. Some of them, however, would deem it conceivable to remove the agricultural activities from the scope of the Act of competition in the framework of the block exemption.

Summary

In this paper we study the effect of European and national Competition Law on the agricultural sector.
1. The subject of the first part of this paper is the Hungarian Competition Law. First we describe the legal foundation of national Competition Law. We want to answer to these questions:
1. Which legal basis has the Hungarian legislation for Competition Law?
2. Which instruments exist in the Hungarian legislation for the control of restrictions on competition?
3. Which sanctions are provided for illegal restraints of competition and malpractice?
4. Does the Hungarian legislation differentiate between horizontal and vertical restraints of competition?
5. Are there any exceptions or exemptions to the illegality of horizontal and vertical restraints of competition?
6. Are there any rules concerning recommendations?
7. Are there special provisions concerning the abuse of a dominant market position?
8. Are there any rules referring to discriminatory measures or obstructive competition practices?
9. Are there any rules concerning mergers of companies?
10. Are Competition Law based decisions of government agencies or courts solely focused on aspects of competition, or do they equally take into account aspects of economic and social policy?

In the second place we write on the special provisions for agriculture in Competition Law:
1. Does the Hungarian legislation contain special provisions for farmers or general provisions, which also farmers can invoke.
2. If yes, to which business and products are these special provisions applied?
3. Are there exceptions for horizontal restraints of competition in the agro-sector?
4. Does the Hungarian legislation feature special provisions for cooperative producer organisations?
5. Are there any special provisions for co-operations in the forest sector?
6. Are there exceptions for vertical restraints of competition in the agro-sector?
7. Does the Hungarian legislation accept organisations for special branches of trade?
8. Does the legislation know special provisions concerning leasing agreements for contracts in the area of plant breeding and seed?
9. Does the Hungarian legislation feature the possibility of declaring horizontal or vertical restraints of competition by private organisations and associations as generally binding?
10. Are there any restrictions on exemptions for the agro-sector by a supervisory body combating the abuse of exemptions?
11. Could the agro-sector use more horizontal and vertical co-operations and mechanisms facilitating co-operation, provided by the Hungarian Competition Law?
12. Does the Hungarian legislation know special provisions protecting farmers from discriminatory or obstructive practice?

II. The second part of the paper includes the relationship of the Hungarian Law and EC Law. There we want to answer to these questions:
1. Which conflicts arose until now between EC Law and the Hungarian legislation because of the supremacy of the Community Law?
2. Has the Hungarian legislation been modified due to EC Law or will modifications become necessary in the future?

Bibliography

THE FUTURE IMPACT OF THE ROME CONVENTION ON HUNGARIAN CONFLICT RULES

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Abstract: The article compares the current Hungarian private international law regime to that of the Rome Convention of the EC. While the Convention is before changing into an anticipated Regulation, it makes sense to test Hungarian PIL provisions against the Convention because to a certain extent the Regulation is likely to build upon the regime of the Convention. The paper discusses the different provisions from party choice of law to connecting factors in the absence of choice, from consumer and individual employment contracts to the Convention's Article 7 mandatory rules, from the law applicable to formal validity to renvoi, and concludes that while Hungary's PIL system is something very close to the Convention, several changes – some minor some more substantial – will be introduced into Hungarian law upon the passing of the Regulation. The paper also evaluates the impact the Convention has had on Hungarian PIL so far and assesses whether or not formal modification of the Hungarian law on PIL will be needed.

At the time of drawing up this present study the 1980 Rome Convention on the law applicable to contractual obligations is under transformation into an instrument of secondary EC legislation – a'la the transformation of the 1968 Brussels Convention on jurisdiction and the enforcement of judgements in civil and commercial matters into Council Regulation (EC) No 44/2001. There have been quite many different suggestions as to the new rules of the common European private international law (PIL) in the anticipated Rome Regulation and thus the exact direction of the changes is unpredictable at this point of time. However, since the much anticipated Regulation is very likely to adapt the PIL system of the Convention at least to some extent, it does make sense to sum up the main differences between the existing regime and practice of the Rome Convention and Hungarian PIL in its black letter law, case law and legal writings.

1. Legislative steps to be expected from Hungary

On the one hand the transformation of the Convention into a regulation (or directive) is underway. The document by the Commission that initiated the changes called the Green Paper on the conversion of the Rome Convention of 1980 on the law applicable to contractual obligations into a Community instrument and its modernisation was finalized in 2002. At the core of the Green Paper is a list of questions to be answered before 15 September 2003 and to the discussion in the Green Paper comments were to be made until that date. In fact by now there have been several communications to the Green Paper outlining some desired direction of the changes from both governments and professional organizations. It means that by the time Hungary joined the EU on May 1 2004, legislative efforts to change the Convention into a Regulation had been well underway.

1 COM/2002/0654 final
On the other hand accession to the Convention has been noticeably slow so far.\(^2\)
Therefore it makes more sense for Hungary – and for the new member states joining the EU on the same day as well – to wait until the Regulation is passed than to initiate the circumscribed and lengthy process of joining to and ratifying an undoubtedly outgoing international convention. While there surely will be a great number of civil and commercial contracts in the interim period where the conflict rules of Rome would be relevant, it practice both the PIL of Hungary and its court and commercial arbitration practice are close enough to the rules of the Rome Convention that it will most probably not cause any major obstacle to business transactions in the field where the Rome Convention would apply. It is therefore anticipated that for the time left until the Rome Regulation is passed Hungary will not sign the Rome Convention.

Note on the other hand, that aside the timing of the Regulation, in principle accession to the Convention is a must. This may be the reason why some commentators even recently argue that Hungary should sign the Convention and that the Convention should become part of the law of the country.\(^3\) It is nevertheless more reasonable to expect that nothing like this will take place before the Regulation is passed.

2. The impact of the Rome Convention rules on Hungarian PIL so far and future changes expected in Hungarian PIL

Although Hungary has not signed the Rome Convention, there have been some minor changes that arose from the Rome rules in anticipation of the EU accession. These rather mistakenly implemented changes related to the law applicable to consumer contracts and individual employment contracts and will be discussed under the next title. An important scholarly suggestion has been put forward that – following the example of Finland\(^4\) – the rules of the Rome Convention should be implemented in a temporary nature even before the EU accession, in order to prepare the courts for the application of its rules.\(^5\) The chance to realize this suggestion has gone by now.

As it will be shown, there is a list of subject matters in which current Hungarian PIL does not precisely match the Convention and which will therefore need to be changed. On the other hand it is still doubtful as to what the exact procedure to be followed will be. Since we are talking about a Regulation in principle its rules should be applicable without formal modification of the Hungarian rules. In this case some provisions of the current Hungarian PIL Decree (Decree No. 13 of 1979, hereinafter: Decree) will automatically be outdated but most rules of the law applicable to contractual obligations will survive even if they contradict the rules of the anticipated Regulation.\(^6\) Their 'survival' will, however, be limited to questions outside the scope of the common European PIL. For instance while the Convention excludes renvoi and will most probably do so the Regulation, too, the Hungarian rule that permits remission will continue to apply in the law of persons, property, intellectual property, succession, family law, etc. As for contract-specific questions that contradict the Regulation, they will be recognized for contracts not covered by the Regulation, such as those arising from matrimonial relations.\(^7\)

But it is more likely that with the Regulation a change in the instruments of Hungarian PIL will take place anyway. One reason is that in the beginning of the process of re-codification of the Civil

\(^2\) Suffice it to point at the fact that while the Convention was drafted in 1980 it only entered into force in 1991. It took 11 years for the seven ratification instruments to be deposited with the Secretary-General of the Council as required for entering into force by Article 29 of the Convention.
\(^3\) Burián 2004 68-69
\(^4\) Finland voluntarily took over the Rome Convention rules seven years before becoming a Member State of the EC.
\(^5\) Vékás 2001 258-259
\(^6\) See also Burián 2004 68
\(^7\) Provided, of course, that the Regulation will follow the exclusions of the Convention in its Article 1.2.
The Future Impact of the Rome Convention on Hungarian Conflict Rules

Code, PIL was mentioned. Although it is very likely by now that PIL will not be re-codified within the stream of the re-codification of the Civil Code,\(^8\) the question is not at all forgotten. As with conflict questions outside the Convention in the EC, there is example in Hungary too that PIL extends over the Decree that should contain it.\(^9\) As the new Regulation aims to bring all conflict rules under one instrument, the same should be attempted in Hungary with a new law on PIL. Also, with the new EC Regulation coming out, it is doubtful whether or not it makes sense to leave the contract rules contradicting the Regulation in effect for that slight list of contract questions that the Regulation will not apply to. Also, there are questions outside the conflict rules of contracts that should be conditioned to the needs of today – especially in the light of the fact that no matter how modern and tight, the Decree was enacted in 1979 in a planned economy of a closed society. A lot has changed that should be made into a new law on PIL. Finally, the Hungarian law on PIL, Decree No. 13. of 1979 bears a rather outdated and not very elegant form as to its source, typical of the Communist era. The source is called Decree with the force of an Act of Parliament, which is one contradiction in terms in a rule of law country but not in a closed Communist society. Decrees were passed by the government but their place in the hierarchy of norms was the same as those of Acts of Parliament: hence the name Decree with the force of an Act of Parliament. The need to involve any elected body of legislation in any subject matter was circumvented by the use of such Decrees with the force of an Act of Parliament.

3. Differences between Hungarian PIL and the Rome Convention

Herewith we go along with the differences of the current conflict rules of the Convention and Hungarian PIL. Comparison follows the sequence of the Convention. Issues where there is agreement between the Rome Convention and Hungarian PIL, such as the wide freedom of party choice either expressly or by conduct, the right to modify the choice, public policy, etc. are not dealt with here.

3.1. Contracts with no foreign element. Article 3.3. of the Rome Convention offers basically the same solution to a foreign law choice in a no-international-aspect contract as can be derived from the Hungarian Decree and practice. The leading case is an arbitral decision\(^10\) whereas the only foreign element in the contract was the choice of foreign law by the parties. The decision almost exactly matched the wording of the Rome Convention rule. However in lack of express statutory language there may be several different approaches under Hungarian PIL all leading to the same solution. One approach may be that if there is no other foreign element in the contract than the choice of foreign law clause, the contractual relationship does not fall under the scope of PIL at all, and the choice of law clause is only a brevitatis causa incorporation of foreign law allowed by the civil law doctrine of contractual freedom for dispositive rules. The other approach may be, that even if the only connecting factor is the choice of law clause itself, the contract falls under PIL and matches the category of evasion of law.\(^11\) While the Rome Convention rightly does not undertake to decide for either of the doctrinal approaches, it does offer a normative outcome. Even though it has been the same as the Hungarian case practice and legal doctrine, it is not expressly in our black letter law.

3.2. The existence and validity of the consent to the choice of law. Capacity. The question of existence and validity of the consent has been missing from both Hungarian statutory law and case law. It has also almost entirely been missing from contemporary Hungarian legal doctrine as well.

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\(^8\) Burián 2001 78
\(^9\) To be discussed later is a conflict rule for consumer contracts that mistakenly made its way into the Civil Code.
\(^10\) VB 1998.3.
\(^11\) Note that this approach has been reflected in earlier French doctrine as well under the name fraudé à la loi. E.g. Cass. (civ.) (Feb. 19 1930) and (Jan. 27 1931) S.1933.1.41. Also: Rabel 1960 402, Batifoll (1938) 63
Therefore, it will be a subject-matter re-introduced after a long period of silence. Note that while the question of consent has little court practice to the Rome Convention, in theory there may be a great many differences to consent in different laws that might as well concern the validity of the consent to the choice of law clause. Szászy as early as 1929 listed a line of different approaches concerning the validity or existence of consent to an agreement, may it be the choice of law clause or anything else. For instance, according to some laws fraud may cause the consent invalid regardless of who caused it while other laws stipulate that consent is lacking only if the fraud was caused by one of the contractual parties and not by a third party. There may also be differences in laws whether threat to any third person may be reason to declare the consent lacking for illegal use of force, or whether only if the contracting party personally was threatened can we say that he consented under illegal force; or there may be a certain circle of people whose threatening may cause the consent be invalid, such as parents, relatives, etc.

While Szászy in 1929 found that the validity and existence of the choice of law clause should be determined by the *lex pro voluntate*, it has not been dealt with later. And although the Hungarian Decree also uses the term *choice and parties* and not the civil law term *consent*, the conditions of the civil law term *consent* could as well be deducted from the PIL terms *choice and parties* and we could therefore easily conclude that on the question whether there was *choice* of the *parties*, the law of the forum applies. However it is not the meaning of the Article 3.4. consent rule of the Convention that would not be possible to deduct from Hungarian PIL interpretation rather than the Article 8.2. consent which seems new to Hungarian PIL.

Note that Articles 1.2. (a) and 1.2.(e) exclude questions of capacity therefore if the existence or validity of the consent arises from the question such as the capacity to contract or the representative powers of a company, the Convention does not apply. This is the same solution that Hungarian PIL contains: the *lex obligationis* does not extend to questions of capacity or similar questions of what is called the *About persons* chapter of civil law. On the other hand, the Article 11 solution of the Convention is missing from Hungarian law and will therefore need to be incorporated if kept in the anticipated Regulation.

### 3.3. Applicable law in the absence of choice

The list of connecting factors under the Hungarian PIL Decree looks very much like the one in Article 4. of the Convention. There are, however, significant differences in detail.

As a first step, the Hungarian Decree defines the connecting factor for 13 particularly named types of contracts and names the party whose domicile, habitual residence, seat or branch at the time of the conclusion of the contract determines the applicable law. The parties’ names are, all but one, those who effect the performance characteristic of the contract – and so the list almost meets the characteristic performance assumption test of Article 4.2 of the Convention. The exception is copyright licensing agreements where the contract is tied to the law of the country where the user

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12 For pre-World War 2 discussion in Hungarian doctrine see Szászy 1929 20-25. For a recent publication on the subject-matter see Palásti 2004
13 In the only reported case – a German case – it had to be determined whether a choice of law clause in the general conditions of an order bill of lading was applicable in the case between the insurance company being the plaintiff and a carrier being the defendant. Did the use of the bill of lading amount to consent to the choice of law clause for the contract therein? (II ZR 34/86 Bundesgerichtshof (BGH) • 1986, December 15, at http://www.rome-convention.org) We must add that the case seems to be as much about tacit choice and thus fall under Article 3.1. of the Convention as about the existence or validity of the consent of the parties.
14 Szászy 1929 22
15 Ibid.
16 This is without prejudice to Article 11 on incapacity.
17 See Articles 10-18. of the Hungarian decree
18 Hungarian PIL Decree Article 25.
19 Article 25. c)
of the work is. However, the list also contains carriage of goods without the further qualification that Article 4.4. of the Convention requires. Also: because the Convention directs us to the place of the party who performs the characteristic performance only as a presumption of the closest connection rule of Article 4.1., whereas the Hungarian rule is an outright order to apply the law of the place of the party with the characteristic performance, for all cases where the contract is more closely connected with a country other than the place of the party with the characteristic performance, the application of the Convention leads to another law than the application the Hungarian PIL. As to the place of the person with the characteristic performance, the Hungarian list of domicile or habitual residence for natural persons and seat or branch for companies and other legal entities gives discretion to the judge to decide which of the two factors for a party it will look at. This may easily lead to the application of the law that follows from the stricter wording of the Rome Convention such as 'habitual residence', 'central administration' and the entire second sentence of Article 4.2., but it may as easily lead to the application of a law other than that, provided that it is either the place of domicile, habitual residence, seat or branch. Note that the word 'place of business' is wider than the Hungarian term 'branch' which does not include a place of business in a country other than where the central administration is – called a 'drawer'. This distinction does not, however, come from PIL – it is the way it is used in Hungarian commercial law terminology.

The Hungarian PIL Decree then continues with a list of exceptions alike Article 4.3. of the Convention about immovable property. The first exception is in fact immovable property in the Hungarian Decree as well, but while the lex rei sitae rule in the Convention is just another rebuttable presumption of the closest connection rule, the Hungarian law again contains a direct order to apply the law of the place of the immovable.

The same paragraph of the Hungarian PIL Decree sets forth the loi du pavillon or lex bandi rule for contracts the subject matter of which is registered vessel or plane – a rule that is entirely missing from the Convention. The next set of exceptions refers to contracts that are characterized under Hungarian law as venture contracts in which the person with characteristic performance undertakes to perform a certain activity – as opposed to giving something or abstaining from doing something – which is manifested in a certain guaranteed result. Contracts that belong to here relate to construction, building, engineering, designing, supply of goods to be manufactured, mechanical fixing, etc., and their connecting factor is the law of the country where the activity is to be performed or where the result is to be achieved. No such rule is found in the Rome Convention, albeit at the least it might have been a good presumption of the closest connection against the Article 4.2. presumptions, if the classification of at least a very few named contracts – such as building or engineering contracts – would have been approved. The list of further exceptions that follows in the Hungarian Decree relates to contracts that are excluded from the scope of the Rome Convention by way of Article 1.2. of the Convention.

If a contract does not fall under the list of the 13 named types of contracts of Article 25 of the Hungarian PIL Decree or does not fall under any of the exceptions such as contracts for immovables or registered vessels, the rule of the domicile, habitual residence, seat or branch of the party effecting the characteristic performance in a contract follows. As a last resort, if it is not possible to determine who the party obliged to perform the characteristic performance is, such as the case of very complex contracts where a variety of different kinds of obligations and rights for both parties are incorporated into the same contract, or such as simple exchange of goods contracts like an

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20 Article 26. (1)
21 Article 4.5. of the Rome Convention
22 Article 26. (2)
24 Article 29. first sentence
apple-for-orange type of agreement, the closest connection rule follows.\(^{25}\) Note, that there are no presumptions for this rule: all kinds of elements of the contractual relationship have to be taken into account to find out which country the contract is connected to the most. After all, this is the same fall-back rule that is in the Rome Convention, but while in the Rome Convention all other rules are just rebuttable presumptions for the closest connection test, in the Hungarian law other connecting factors that come before the closest connection fallback rule are irrebuttable directions to apply the law indicated therein.

Finally, the conduct to be followed to check and evaluate the delivery of the goods or services by the receiver upon delivery and the way to object upon receiving the delivery is determined by the *lex loci solutionis* of any contract\(^{26}\) - a rule that is entirely missing from the Rome Convention.

3.4. Consumer and individual employment contracts. The only change that has been made to Hungarian PIL arising from the Rome Convention was to bring its conflict rules for consumer and individual employment contracts in line with the Convention. However as it has been pointed out many times by commentators\(^ {27}\), these attempts partly failed. The changes the extent to which the Rome Convention model was followed included the concept of consumer contracts\(^ {28}\) and the Article 5.2. connections between the habitual residence of the consumer and the fact pattern\(^ {29}\); the extension of party autonomy to individual labour contracts,\(^ {30}\) the objective connecting factors of individual employment contracts\(^ {31}\) as they are in the Rome Convention\(^ {32}\) and a reference to the mandatory rules of the *lex laboris* as a limit to party autonomy.\(^ {33}\) However this setting is far from perfection. On the one hand, the PIL Decree only designates the law of the habitual residence of the consumer if there was no choice of law by the parties.\(^ {34}\) In other words according to the PIL Decree the law of the habitual residence of the consumer does not limit party autonomy by its mandatory rules, only serves as an objective connecting factor in the absence of party choice. What limits party choice is a small rule in another Decree that enacts certain modifications to the *Civil Code*. Article 5/C of the No. 2 Decree of 1978 refers to the PIL Decree and prescribes the use of Hungarian consumer protection rules if, and only if the law of Hungary would be the applicable law in lack of party choice. This solution has deserved much criticism from commentators.\(^ {35}\) On the one hand, nothing justifies the placing of a conflict rule – the only conflict rule – in a law about substantial civil law. On the other hand – and as to substance this is the stronger criticism – the whole concept of mandatory consumer protection is frustrated by allowing it to apply only to consumers who live in Hungary. The same one-sided protection is applied for labour contracts: the mandatory provisions of the *lex laboris* apply only if the law applicable to the contract would be Hungarian law.\(^ {36}\) Further, some other connecting factors incompatible with the Convention have remained in Hungarian PIL for special types of labour relations such as the case when both the employer and employee have the same *lex personae* and the employer is a foreign state\(^ {37}\) – a specific rule for diplomats and foreign employees on embassies – or another for sailors and stewerdesses: a job upon vessels and planes.

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\(^{25}\) Article 29. second sentence

\(^{26}\) Article 30. (2)

\(^{27}\) Burián 1999, Burián 2004 66-67, Vékás 1999

\(^{28}\) Paragraphs (2) and (3) of Article 28/A of the Decree

\(^{29}\) Article 28/A (1) of the Decree

\(^{30}\) Earlier it was not possible to designate the applicable law to employment contracts by the parties at all. The change was brought about only as a direct consequence of the Rome Convention rule and the Decree was modified and permitted party choice for employment contracts as well.

\(^{31}\) Article 51 (2) of the Decree

\(^{32}\) Article 6.2. of the Convention

\(^{33}\) Article 51 (3) of the Decree

\(^{34}\) Article 28/A (1) of the Decree


\(^{36}\) Article 51 (3) of the Decree

\(^{37}\) Article 52 (2) of the Decree
where the connecting factor is the *loi du pavillon*.\(^{38}\) These rules may be taken as indicator or presumption for the place where the employee carries out his work – such as the work on a vessel shipping under a certain flag – or presumption for the closest connection rule that the Convention uses as a last resort.\(^{39}\)

Quite soon the lacking adoption of the specific rules on consumer contracts and individual employment contracts will have to be completed.

### 3.5. Mandatory rules under Article 7

Article 7.1. will be difficult to fit into traditional Hungarian PIL.\(^{40}\) So far as Article 7.1. is used to direct the judge to take into consideration foreign public law provisions – such as export controls, competition rules, customs rules, revenue and fiscal laws, etc. – considering them *mandatory rules* in the sense of Article 7.1., the entire spirit and doctrine of Article 7. goes against traditional Hungarian PIL thinking. The reason is, that according to Hungarian PIL the rules of private international law apply only if there is conflict between private law rules.\(^{41}\) That there would be competing legal systems for public law issues is outside the scope of PIL. While systems that do not differentiate between private and public law consider conflict of laws to resolve the conflict of any laws, and the application of some foreign public laws such as criminal or revenue or other kinds of laws is excluded only as a subject matter of public policy within PIL.\(^{42}\) Hungarian PIL does not address the issue at all.\(^{43}\) There may be very particular areas or instruments of law outside of PIL that deal with conflict-like situations that resemble the traditional PIL conflict, but they do not form a separate branch of law. Such small areas are the part of financial law that deals with double taxation, particular laws on the recognition of titles obtained abroad, bilateral or broader international agreements to facilitate the use each other's procedural rules for obtaining evidence or conducting hearing abroad in criminal matters, etc.

It is nevertheless possible to take foreign public law rules into consideration but only if they either may come under any term of the applicable substantial law, such as a reference to good morals of the society,\(^{44}\) or if the applicable law contains no good-morals or like clause but the *lex fori* does, the breach of foreign public law provisions would go against a domestic rule of public policy force, such as the one on the protection of good morals.

As to Article 7.1. mandatory rules when they are private law norms\(^{45}\), it will be a great new possibility to label some laws as such even if they do not reach the level of *ordre public*. There have

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38 Article 52 (3) of the Decree
39 Article 6.2. (b) of the Convention
40 At the time when signing the Convention was still on the agenda – at least in scholarly circles – Vékás contemplated whether or not it would be desirable to have a reservation against the application of Article 7.1. Vékás 2001 260
41 Article 1 of the Decree names three areas of law in which PIL resolves conflicts: civil law, family law and labour law. Conflicts in no other branches are subject to PIL. See also Burián-Keckés-Vörös 2004 41-51, Mádl-Vékás 1992 43-53
42 See, e.g. Huntington v. Atrill [1893] AC 150 Privy Council; Banco de Vizcaya v. Don Alfonso de Borbon y Austria [1936] 1 KB 140 K.B. Division; USA v. Inkley [1988] 3 WLR 304 Court of Appeal; Peter Bucham Ltd. and Macharg v McVey [1955] AC 516 High Court of Justice of Eire
43 And the situation is very much alike in some other legal systems that make a distinction between private and public law.
44 Such as the famous Nigerian masks case in Germany, where folklore masks were illegally smuggled out of Nigeria and the question was whether the Nigerian ban was of any relevance for the insurance contract in which insurance of the smuggling goods was provided for. The German solution was that the breach of the foreign exportation laws went against the good morals clause of the German law. (BGH 22.6.1972 NJW) The question can be formed more generally for any contract the subject matter of which is smuggled articles from a third country. Note that the Hungarian Civil Code contains the same good morals clause (Civil Code Article 200. (2)), and so if the applicable law is Hungarian, on the grounds of good morals we may give some private law effect to foreign public law rules. Because this clause seems to be one of public policy relevance, if the applicable law is not Hungarian but the forum is in Hungary, we may still come to civil law conclusions of breaking the foreign law export bans, like invalidity of the contract. Other such clauses may be a general duty of good faith or fairness in the applicable law (for Hungarian both are in Article 4. (1) of the Civil Code) all applicable against the breach of a foreign public law such as a ban on exports of certain articles.
45 Such as rules in many jurisdictions that protect against unfair contractual terms. More specific rules are those limiting the exclusion of liability for a carrier like the Hague-Visby Rules. (See The Hollandia [1983] 1 AC 565 House of Lords;
been particular situations in the past when achieving a particular political goal included particular civil law modifications that could easily be frustrated by a foreign choice of law clause. Such good example was the stricter contractual conditions for agricultural land use contracts for land in Hungary with foreign tenants which aimed at protecting against disguised illegal sale of agricultural land to foreigners. The stricter contractual conditions imposed upon this particular contract could easily be side-stepped by a choice of law clause. Article 7.1. mandatory rules could lead to the application of some of the private law provisions other than the one chosen and safeguard some sensitive objectives – such as those prescribing greater strictness in contracts with foreigners over agricultural land use in Hungary.

Finally, the Article 9.6. mandatory rules on formal requirements of contracts in immovable property is not expressed in the Hungarian Decree, but in principle the rule is practiced with the same content for so long as the property is in Hungary and the formal requirements have an element of a public law obligation, such as to register the land with the respective authority. As to private law formal requirements however, such as to have the contract in writing, even if the local rules set forth obligations of form to the contract, a simple foreign choice of law clause can validate contracts if the contract meets the formal requirements of the chosen law but not the lex rei sitae.

3.6. Formal validity. The rules of the Convention on formal validity more or less correspond with Hungarian PIL setting: the old tradition of the lex loci contractus applies in both Hungary and the EC. There are some minor differences, however. One is that the Hungarian Decree makes no difference between contracting with the presence of both parties in the same country or contracting from remote states. It is therefore left to practice and theory whether a contract that is concluded between parties in different countries has a lex loci contractus or not. Secondly, the agent-rule of Article 9.3. of the Convention is missing from the Hungarian Decree, although it would be hard to interpret the Decree differently. The Article 9.4. rule of the Convention about an act intended to have legal effect is slightly different in Hungarian PIL: while Article 9.4. allows the law of the place where the act was done to formally validate the act, Article 30 (3) of the Hungarian decree allows the law of the place where the intended legal effect should take place to do the validation. These two may be different countries: for instance when a notice under a contract that a receiver of cargo is able to receive the cargo at the destination is sent from the seat of the company in one country but receiving the cargo would take place along the way of the cargo in another country, the validating rule under the Convention would be the seat of the company while it would be the law of the place where receiving the cargo would take place under Hungarian PIL. Finally, it is not even clearly stated in the Decree that the validating rule would apply to any act not just a contract, although it depends on interpretation whether any act under an existing or contemplated contract may come under the wide notion of contract.

3.7. Assignment and subrogation. While the main contention to include both assignment and subrogation under the lex obligationis of the contract from which they arose is the same in Articles 12-13. of the Convention as in Article 30. (1) of the Decree, the kind of 'just-in-case' detailed description of what is meant under these headings that is contained in the Convention is missing from the Decree. No wonder however – this should rather be a question of characterization which is conducted according to the notions of the lex fori and not a matter of conflict of laws. Note, that the


Palásti 2001

Article 9

Article 30. (3) of the Decree

Article 9.1. of the Convention

Article 9.2. of the Convention
3.8. Burden of proof. The burden of proof provision of Article 14. of the Convention may conflict with existing Hungarian PIL if a certain question concerning proof or taking evidence is characterized as a procedural matter, in which case the *lex fori* should apply. According to the Convention however, if a certain method of obtaining evidence exists in the *lex obligationis* or in any law that is used for formal validity and that method can be administered by the forum, that method may be used as evidence.\(^{51}\) Note that the *public policy* clause may still obstacle the use of some forms of evidence which are not known to the forum. An example is the taking of an oath which hardly seems to be of any value in the process of evidence in Hungary even if the chosen law contains it as a means of evidence. In this sense according to Article 14. of the Convention an oath could be used in the way of taking evidence but public policy considerations may bar an oath from bearing any relevance in Hungary.

3.9. Renvoi. Article 15 of the Convention excludes renvoi for all possibilities. Article 4 of the Hungarian PIL Decree denies transmission but allows remission. While most legal writers agree however that even remission is not possible for party choice of law, there is no denial of remission for connecting factors in lack of party choice. Since as we have seen the Hungarian connecting factors for the absence of party choice of law are slightly different than in the Rome Convention a remission situation is easily thinkable, especially for certain types of contracts where the characteristic performance test of Article 4.2. of the Convention does not meet the Hungarian connecting factor, such as licensing contracts under copyright law or building or construction or engineering contracts. As an example, if there is no choice by the parties, a software end-user licensing agreement for a software downloaded by a user living in a Rome Convention country from a Hungarian site offering the software of a company with its central administration in Hungary, according to Article 25 c) of the Hungarian Decree the contract would be governed by the law where the user is domiciled which would refer the case back to Hungarian Law\(^{53}\) and thus remission is accepted. If a contract to design a building which is to be built in a Rome Convention country is between a designer seated and designing in Hungary and a company in a Rome Convention country, according to Hungarian PIL the law of the Rome Convention country would apply\(^{54}\), which by virtue of Articles 4.1. and 4.2. would refer the case back to Hungarian law. A Hungarian court would accept such remission.

Note, that while Hungarian legal writing does exclude the possibility of remission for party choice, it does not follow from the Decree itself. And while it is clear that if the parties chose a certain law to apply to their contract, the connecting factors of that law for the contract in the absence of choice are not relevant for renvoi, it does make sense to consider the possibility of renvoi for party choice of law. Under the Rome PIL regime this is the case when different tests are applied to determine party choice by conduct. For example there is case law in some Rome Convention countries to determine silent choice upon the use of legal texts or reference to legal sources of a certain jurisdiction or language use\(^{55}\) which may not be regarded so in Hungary. Thus, the choice of the French law was inferred from the fact that the contract referred to French enactments relating to the

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\(^{51}\) Article 14, of the Convention
\(^{52}\) Burian-Kecskes-Voros 2004 215, Madl-Vekas 1982 419
\(^{53}\) Articles 4.2. and 4.3. of the Rome Convention
\(^{54}\) PIL Decree Article 26. (2)
\(^{55}\) E.g.: Societe Lorraine des Produits Metallurgiques (SPLM) c/ SA Banque Paribas Belgique Korenmarkt et Soc. BVBA Finecco, Cour d'appel de Paris, 1ere chambre, section des urgences. • 1993, November 10; Giannantonio v. Societe Imprese Industriali s.p.a., Pretura di Milano (Pret. Milano) • 1995, January 5; XI ZR 42/96 Bundesgerichtshof (BGH) • 1997, January 28; VII ZR 19/98 Bundesgerichtshof (BGH) • 1999, January 14
securities; Italian law was found to apply by silent choice because in an employment contract the dismissal for cause is described with the same words as an Italian law does and also regulations of various aspects of the work relation are similar to Italian law; or: the conclusion of a contract between German nationals in Germany in German language has to be considered as an implied choice of German law; or an agreement that a contract has to be governed by German contracting rules for award of public work contracts (VOB) and some of the general German standards for construction works (DIN) has to be regarded as a inferred choice of law by the parties, etc. However it may rather be so that such indicators will only be taken as incorporation of foreign law or simple language use questions and will not justify a tacit choice. Therefore, if in a contract that refers to the Hungarian Civil Code and may as well be in Hungarian the test of silent choice for the Hungarian judge leads to the application of a Rome Convention country – because, maybe the contract is to be preformed there and may have been signed there as well – and in that country the use of Hungarian laws and language in the contract is an implication of a choice of Hungarian law, remission to Hungarian law would be possible under Article 4. of the Hungarian PIL Decree yet impossible under the Rome Convention.

4. Conclusions

To the extent the PIL regime of the Rome Convention is relevant for determining the future PIL rules of contracts in the EC, Hungarian PIL is more or less coherent with those rules. There will nevertheless have to be certain changes in Hungarian PIL in questions regarding the existence and validity of the consent to a choice of law; applicable law in the absence of choice; consumer and individual employment contracts; mandatory rules; formal validity and capacity; burden of proof and exclusion of renvoi. The changes will most probably not take place by signing the Rome Convention but will wait until the common European PIL takes another regulatory form.

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THE EUROPEAN CONTROVERSY
IS THE EU A TRUE COMMUNITY OF CULTURES?

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The main focus of my Ph.D training is the preservation of cultural heritage. Within this topic I pay attention to three main fields: historical preservation in Hungary, in the European Union and the world heritage. In my first year as a postgraduate student I was able to analyze the history and the development of this protection in Hungary. After studying the history of Hungarian national historic monuments, buildings and current legislation I came to the conclusion that the aforementioned fields were established long after they had been in Western-European countries. That is why I have decided to look for inspirations and samples for comparison from the European Union.

It is rather evident to the wide public, that the European Union is an economic and political community. It is however quite an intriguing task to examine if it is truly a community, a community of different cultures. With the help of scholarly comparison of the initial ideas stemming from the founders of the European Union and the present state of culture I expect to find some answers pertinent to this question in this article. By giving the European Union a say in cultural matters, the Member States’ governments set out to create a 'Europe of the peoples'. According to this idea they want to make people in Europe aware of their shared history and values but at the same time the local and regional cultures must be cultivated also. More specifically, the point was to encourage cultural exchanges within Europe by establishing European projects to inspire creativity and to make culture accessible to the greatest possible number of people. I hope that by this paper I can prove that the European Union is more than an economic or political community.

Introduction

It is rather evident to the wide public, that the European Union is an economic and political community. It is however quite an intriguing task to examine if it is truly a community, a community of different cultures. With the help of scholarly comparison of the initial ideas stemming from the founders of the European Union and the present state of culture I expect to find some answers pertinent to this question.

The Maastricht Treaty gave the European Union powers of its own in the sphere of culture for the first time.

'Marking a new stage in the process of European integration undertaken with the establishment of the European Communities.' 'Creating an ever closer union among the peoples of Europe'\

According to this the genuine intention appeared to be to create a 'Europe of the peoples' by using culture as a 'vehicle' for it. Different as they are, the peoples of Europe share the same history, which gives Europe its place in the world and which makes it so unique. Despite geographical, religious and political differences, the artistic, scientific and philosophical currents of past

¹ These are taken from the preamble to the Treaty on European Union, signed in Maastricht in 1992.
centuries have influenced and enriched one another in a way, which enabled a common heritage for the many cultures of today’s European Union.

The ’European cultural model’ involves respect for each peoples’ culture and for the interplay between them, but at the same time encouraging forms of cooperation which can enrich each culture.

The Maastricht Treaty was not content with making culture a fully-fledged aspect of European action. It also made it incumbent on the EU to take cultural matters into account in all its policies. The financial assistance which the EU makes available under its social and regional policies also means that Europe is a significant player in terms of cultural development.

One of the most pertinent questions is: how can the EU encourage the ’cultural dialogue’ between the peoples of Europe. By establishing projects and networks, to make all sides aware of how the cultural and creative processes works, and to encourage all the peoples of the EU to develop different forms of cultural expression.

Since 2000 the EU has had its first framework program devoted entirely to cultural matters, named ’Culture 2000’. This is the cornerstone of the EU’s cultural activity. With a budget of EUR 167 million over four years this program is rather modest in terms of the EU’s overall expenditure. It should, however be emphasized that a large number of other EU policies, touch upon culture in a broader sense.  

II. ’Culture 2000’ Program

The aim of the ’Culture 2000’ program- which combines the old ’Raphael’, ’Kaleidoscope’ and ’Ariane’ programmes- is to develop a common cultural area by promoting
- ’cultural dialogue’
- knowledge of the history
- creation and dissemination of culture
- the mobility of artists and their works
- European cultural heritage
- New forms of cultural expressions.

The program supports transnational cooperation projects which involve the cooperation between creative artists, cultural operators and the cultural institutions of the countries participating in the program.

The in-depth consultations undertaken by the Commission- as part of the preparation of the framework programme - clarified the role of culture in meeting the great challenges now facing the European Union. 

Since the Treaty on European Union was signed, the Community has taken a number of initiatives, these are the followings:

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2 Amounting to at least EUR 500 million per year
3 regional and social policies, education and training, scientific research programmes and so on.
5 It is for the above reasons that culture is closely associated with the responses that are needed to meet major contemporary challenges, such as the acceleration of European integration, globalisation, the information society, employment and social cohesion.
shown that, apart from its achievements in the economic and monetary fields, the European project extends to the entirety of European society and must involve European citizens to a greater extent;

- started to integrate the cultural dimension into those of its decisions which have an impact on culture;
- implemented the first three programmes encouraging cultural cooperation in the arts (Kaleidoscope), literature (Ariane) and heritage (Raphael);
- helped develop relations between culture, the culture industries and employment, on the basis of the Commission's work showing the importance of cultural activities in society and the potential for job creation that they represent.

The 'Culture 2000' programme is a single programming and financing instrument for the period from 1 January 2000 to 31 December 2006. The Programme emphasises that the role of culture as an economic factor and as a factor in social integration and citizenship. The Culture 2000 programme furthers a linkage with other Community policies which have cultural implications.

The programme's objectives are achieved by the following actions:

- specific innovative and/or experimental actions involving operators from at least three participating countries. These actions aim mainly to encourage the emergence and spread of new forms of cultural expression, improve access to culture, in particular for young people and the underprivileged, and promote live broadcasting of cultural events using the new technologies of the information society;
- integrated actions covered by structured, multiannual cultural cooperation agreements. These agreements are between cultural operators from at least five participating countries and their aim is to create, within a period of up to three years, structured cultural actions which help to achieve an objective of cultural interest which has been set in advance. The cooperation agreements relate either to enhancing a cultural field or to integrating several cultural sectors;
- special cultural events with a European and/or international dimension. These events must be substantial in scale and scope and must help to increase the sense of belonging to the same community (such as the "European Capital of Culture" initiative).

The funding for the implementation of the Culture 2000 programme for the period 2000-2006 is EUR 236.5 million. This budget is broken down as follows:

- a maximum of 45% for specific innovative and/or experimental actions;
- a minimum of 35% for integrated actions;
- 10% for special cultural events;
- 10% for other expenditure.

The Commission is responsible for implementing the Culture 2000 programme, assisted by an advisory committee. Member States may use Commission financial assistance to open cultural contact points on a voluntary basis. These are responsible for promoting the programme, facilitating access to it and encouraging participation, and also for providing an efficient link with the various institutions providing aid to the cultural sector in the Member States.

Operators from 30 European countries are currently participating in the "Culture 2000" Programme: the 25 Member States of the European Union, the three countries of the European Economic Area (EEA - Iceland, Liechtenstein, Norway) and the candidate countries (Bulgaria and Romania).

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6 Austria, Belgium, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Slovakia, Slovenia, Spain, Sweden, United Kingdom
By 31 December 2005 at the latest, the Commission will present to the European Parliament and the Council a detailed assessment of the results obtained by the "Culture 2000" Programme. This will allow Parliament and the Council to consider the proposal for a new framework programme, announced for 2004 and planned to start in 2007.

According to the Report on the implementation of the "Culture 2000" Programme in the years 2000 and 2001, the "Culture 2000" Programme has made an exceptional contribution to cultural cooperation in Europe. In 2000 and 2001, more than 1,600 applications were submitted under the programme and almost a quarter received funding. Most of the cultural operators receiving funding were relatively small, in terms of organizational capacity (budget and staff). The funded projects were managed by a wide variety of organizations (NGOs, national cultural institutions, private enterprises, etc.).

The requirement, introduced in 2001, that all co-organisers had to provide 5% of funding helped to ensure that all cultural operators were actively involved in the projects, although it may have prevented the creation of partnerships with no prior history of cooperation and deterred some cultural operators in the associated countries from participating in the programme. Moreover, the number of applications fell significantly in 2001. The five countries which received most funding were France, Italy, Germany, Belgium and Spain. With the exception of Liechtenstein, all participating countries opened a cultural contact point.

III. Other programmes related to culture

Various aspects of culture are taken into account in the development of the European Union's activities relating to audiovisual policy, regional development, employment and training, research and technological development, agriculture, the information society, tourism and business.

**Culture and audiovisual media**

The European Commission runs the Media Plus programme (2001 - 2005) with the objective of making the European audiovisual industry more competitive in terms of training for professionals in the audiovisual industry and the development, distribution and promotion of European audiovisual works. Moreover, following the adoption of the Television Without Frontiers Directive in 1989, a legal framework for the free movement of television services in the EU has allowed the development of a European television market and related services, such as television advertising and the production of audiovisual programmes.

**Culture and regional development**

In order to achieve maximum economic and social cohesion, the European Union takes action using the Structural Funds. It also finances projects to reduce the lag in the development of certain regions in the European Union. These funds are available for regional development.

The aim of the three programmes, which take up 94% of the budget available under the Structural Funds (including the European Social Fund), is to improve growth, employment and regional

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7 Report from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions.
9 European Regional Development Fund, European Social Fund, Financial Instrument for Fisheries Guidance, European Agricultural Guidance and Guarantee Fund
competitiveness and to ensure balanced development of the territory. They are based on three objectives:

- targets the regions whose development is lagging behind;
- supports the economic and social restructuring of areas in structural difficulty outside Objective 1 regions;
- supports training measures outside Objective 1 regions.

In the guidelines for the period 2000 - 2006, the European Commission asks Member States to promote cultural development with a view to job creation potential, as culture not only allows a region to assert its identity but also to develop its tourism potential. Moreover, job creation in the cultural sector is not insignificant and it helps to develop certain activities such as online services and the media.

The four Community initiatives: Interreg III\(^\text{10}\), Urban\(^\text{11}\), Leader \(^\text{+}\)\(^\text{12}\) and Equal\(^\text{13}\) also encourage cultural projects. The innovatory projects encourage local and regional actors to cooperate in various areas of common interest which may be focused on cultural development.

**Culture and human resources**

Since the entry into force of the Amsterdam Treaty on 1 May 1999 and the confirmation that employment is a matter of common interest to the Member States, the European Union has had a proper employment policy which targets the cultural operators among others. The Union has also adopted the European Employment Strategy which also underpins European activities relating to employment. Training of staff in the cultural sector is mainly done through structural operations under the European Social Fund.\(^\text{14}\)

The European Union's education and training measures are available to teachers, pupils and students from all disciplines and other professionals interested in culture. For example, the Socrates programme encourages mobility among students, schoolchildren and teachers within the European Union. The Leonardo programme promotes vocational training, while the Youth programme encourages young Europeans to carry out cultural projects. The Jean Monnet Project supports universities wishing to set up courses on European integration, and the Robert Schumann Project promotes training for members of the legal profession in the various aspects of European regulations.

**Culture and research and technological development**

Research and technological development also reflect the European Union's cultural choices. The aim of the Sixth Framework Programme\(^\text{15}\) is to increase the competitiveness of businesses and to make research available for public use.

Certain priority research themes focus their resources on projects relating directly to cultural activities. Under the "Citizens and governance in a knowledge-based society" a budget of EUR 225 million is earmarked for mobilising European research capacities in economic, political and social sciences and humanities that are necessary for developing a knowledge-based society.

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10. cross-border, transnational and interregional cooperation
11. the regeneration of towns and cities in crisis
12. local rural development
13. transnational cooperation in countering all forms of discrimination and inequality as regards access to the labour market
14. The European Social Fund finances employee training measures under Objective 3 of the Structural Funds and the Equal initiative.
15. for research and technological development (2002-2006)
Culture and agriculture

Although the Treaty provisions on implementing the common agricultural policy (CAP) do not explicitly relate to cultural activities, it must be remembered that agriculture is an integral part of European culture. Moreover, the provisions promote traditional forms of production, preservation of the cultural heritage and the creation of jobs relating to culture.

Information society

The emergence of new information technologies brings with it new methods of work in the cultural sphere. The European Commission wishes to encourage the application of these new instruments to culture. In addition to the ‘User-friendly Information Society’ research programme, the ‘eEurope’ initiative is designed to bring the information society closer to the European public. Action programmes have been adopted for administration and education.

The ‘eContent’ programme supports businesses and administrations wishing to improve access to information from the public sector, enhance multicultural content and increase the dynamism of the digital content market. The ‘eLearning’ programme supports the development of use of the Internet and multimedia in educational and training institutions.

Culture and environment

The preservation of natural habitats as cultural heritage is encouraged by the environmental financial instrument LIFE III and by European environmental regulations.

Culture and tourism

Although tourism may be regarded as one of the areas most closely linked with the area of culture, the European Union’s powers in the field of tourism are very limited. Only major activities may be carried out under the Structural Funds.

Other European Union measures to promote culture

Every year since 1989, on the initiative of the European Parliament, the European Commission has provided funding for town twinning, in order to develop exchanges between citizens and hold seminars and conferences. These exchanges may be cultural in nature.

IV. Heritage protection

The European Union’s works on preserving and conserving the cultural heritage nowadays covers the built heritage, the environment, artistic objects and works, and the non-material heritage. There is no doubt that for example Roman remains or a site of exceptional natural beauty are important not just for the people who live nearby, but for all the people of Europe. These values are parts of our common European heritage.

Conserving the cultural heritage of the peoples of Europe is a prime concern of the Euroregio association in Belgium. Whether the subject be archeology, ethnography or folk traditions Euroregio also collects filmed documents.

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16 ‘eContent’
17 ‘eLearning’
18 The LIFE III financial instrument was created in order to support environmental projects and preserve natural habitats.
The 'Culture 2000' Programme devotes a third of its budget to such conservation projects with a view to make the peoples aware of their common heritage.

Besides 'Culture 2000', the European Union has a wide range of other instruments for use in its heritage conservation work. The Regional Development Fund supplies substantial amounts of money for regional developments aid projects.\(^{19}\)

I have to add that the EU’s environment work can also be used to support projects which have a cultural dimension. Let me show an example: Carnac, in France, is the most important site in Europe for megaliths. This place is highly attractive for tourists, but has become a ‘victim’ of its own success because the flow of visitors has grown into a flood. With the help of the LIFE environment programme\(^{20}\) they could make tourists more aware of the damage they themselves might cause.

It is a commonplace that the tragic events of 11 September 2001 marked the beginning of a new era in the course of international affairs, and ended a period of general optimism generated by the fall of the Berlin wall.\(^{21}\) According to some scholars of international law, it is also having “shattering consequences for international law” by “disrupting some crucial legal categories.”\(^{22}\) The aim of the present study is to emphasize the importance of the adherence to the rules and principles if international law in shaping the response to cross-border terrorism. In this regard special attention is given to the legitimacy of coercive or forcible measures carried out by one or more States invoking the inherent right of individual and collective self-defence. The author strongly believes that contemporary international law poses several limitations on State action in this field, and these limitations should not be disregarded or even abolished for short-term interests, especially when the present state of international law provides satisfactory solutions to most of the emerging problems.

I. The Realm of International Law

From time to time situations occur when subjects of international law violate or threaten rights or interests of other States regarded by the latter as essential. In such circumstances States are tempted to deny the relevance of international law as a compulsory set of rules relating to their actions. Attempts to justify this stance were made using three main arguments.

According to the most straightforward reasoning these exceptional situations, including that of self-defence, must by their very nature escape legal regulation. Such meaning was given e.g. to the US note of 23 June 1928 concerning the Kellogg-Briand Treaty for the Renunciation of War\(^{23}\) by Philip C. Jessup.\(^{24}\) The same point of view was taken by Dean Acheson who, speaking of the propriety of the Cuban quarantine, declared that “the survival of States is not a matter of law” although the United States was influenced by legal principles in “choosing an action consistent with ethical restraint.”\(^{25}\) However, this issue should not be dealt with here in detail since the notion of the existence of extreme situations not covered by international law is supported neither by State practice nor by doctrine. It will suffice to point out that as far as the reaction to the terrorist attacks

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19 For example Greece has launched an ambitious EUR 605 million cultural programme covering the period 2000-06, two-thirds funded by the European Union, one of its aspects being the preservation of the archeological heritage, more especially by modernising museums and museum outreach services.

20 It ran from July 1994 to January 1999.

21 See e.g. Ramonet, Ignacio: *Le nouveau visage du monde*. Le Monde diplomatique No. 573 (décembre 2001)

22 Cassese, Antonio: *Terrorism Is Also Disrupting Some Crucial Legal Categories of International Law*. www.ejil.org/forum_WTC

23 “Every nation is free at all times and regardless of treaty provisions to defend its territory from attack and invasion and it alone is competent to decide whether circumstances require recourse to war in self-defence.”


of 11 September 2001 are concerned, the United States has always asserted that it is exercising its inherent right of individual and collective self-defence in accordance with Article 51 of the UN Charter. The letter of John D. Negroponte, representative of the US to the United Nations, dated 7 October 2001 addressed to the UN and to the Security Council in particular clearly shows that the United States acknowledges the existence of rules pertaining to self-defence and regards its actions as being in accordance with those rules. The same approach was adopted by the North Atlantic Council, the European Council, and by the Committee for Follow-up to the Twenty-fourth Meeting of Consultation of Ministers of Foreign Affairs acting as an organ of consultation in application of the Inter-American Treaty of Reciprocal Assistance (Rio Treaty).

Notwithstanding the fairly unequivocal state of international law in this regard one must add that the advisory opinion of the International Court of Justice on the legality of the threat or use of nuclear weapons rendered on 8 July 1996 might be construed in a way to provide for a special regime in extreme cases of self-defence:

97. Accordingly, in view of the present state of international law viewed as a whole, as examined above by the Court, and of the elements of fact at its disposal, the Court is led to observe that it cannot reach a definitive conclusion as to the legality or illegality of the use of nuclear weapons by a State in an extreme circumstance of self-defence, in which its very survival would be at stake.

The exact meaning of these passages is somewhat obscure. The Court’s inability to reach a definitive conclusion might be attributed to the fact that such extreme situation is not apt for legal regulation or simply to the ambiguous and diverse principles and rules of international law. The arising questions need not be answered at this point since no reasonable person would argue that the very survival of the United States was at stake in connection with the attacks of 11 September 2001.

Another possibility for the exclusion of the situations regarded as self-defence from the scope of international law is presented by the natural law doctrine according to which the origin of self-defence can be traced back to the right of self-preservation or some other fundamental right of States existing independently of accepted sources of international law. The inadequate draftsmanship of Article 51 of the UN Charter, which speaks of an inherent right or droit naturel, might have contributed to the survival of such obsolete view. This attitude has been criticised by many authors, most eloquently by Schwarzenberger and Schachter, and has been clearly rejected by the International Court of Justice:

it is hard to see how this can be other than of a customary nature, even if its present content has been confirmed and influenced by the Charter.

The most annoying effect of the natural law doctrine is that it distorts the true nature of self-defence and other circumstances precluding wrongfulness. Natural lawyers usually regard self-defence as a right and a situation of self-defence or a state of necessity as a conflict between two subjective rights. As a matter of fact self-defence can only be invoked to preclude the wrongfulness of a prima facie illegal act. Self-defence is not a right but a justification for an action taken in breach of the relevant international obligations.

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29 This mistake is made not only by natural lawyers. See e.g. Kunz, Josef L.: Individual and Collective Self-Defense in Article 51 of the Charter of the United Nations. 41 AJIL (1947) 876.
The question, however, still remains that who is entitled to rule on the legitimacy of the actions taken under the pretext of self-defence and whether the legitimacy of such action is justiciable at all. States getting involved in self-defence have often contended that they themselves are the sole and final judges of the lawfulness of the actions taken in self-defence. Should this argument be accepted, it would effectively render useless any legal concept of self-defence. But fortunately it has never received much support. Since Lauterpacht’s classic work it is generally recognized that justiciability is an essential component of the legal character of self-defence.\(^{30}\) States and international organizations have always reserved the right to announce on the legality of actions taken in self-defence, and, in case of abuse, to determine its legal implications \textit{vis-à-vis} the delinquent State.\(^{31}\) The importance of this view was also reinforced by the Nuremberg Tribunal declaring that whether action taken under the claim of self-defence was in fact aggressive or defensive must ultimately be subject to investigation or adjudication if international law is ever to be enforced.\(^{32}\)

States are not very likely to accept the compulsory jurisdiction of an international tribunal in matters relating to the use of force. In consequence recourse can only be made to the international community. The significance and effect of community judgement, however, should not be underestimated.

\section*{II. The Sources of International Law}

After establishing the relevance of the rules of international law governing the use of force in cases of self-defence, we may now turn to the sources of these rules. In this process one must inevitably examine Article 51 of the UN Charter. States have always been uncomfortable with Article 51 claiming that it has never reflected the essential content of general customary law and furthermore it unnecessarily restricts the governments’ freedom of action. Various attempts have been made to downplay this article by ascribing to it a purely declaratory meaning or by interpreting its terms in an extremely broad sense. According to a very popular view, Article 51 left unaffected the traditional justifications for recourse to force accepted by customary law thus self-defence might be invoked in protection of several substantive rights besides being a response to an armed attack.\(^{33}\) Some refute this idea by calling into attention that Article 51 and customary law are basically identical\(^{34}\), others suggest that pre-existing customary law was replaced in its entirety by the provisions of the UN Charter relating to self-defence.\(^{35}\)

The correct interpretation of Article 51 is probably somewhere in between. In the author’s opinion Article 51 has a general scope so that it governs all the situations in which a State might plead self-defence. But it neither replaces nor restates pre-existing customary law concerning the justifications for the use of force. It should rather be considered a rectification thereof in matters expressly mentioned in the text. This approach has several implications as regards the forcible measures taken against international terrorism.

First of all, it creates a close link between the general prohibition of the threat or use of force embodied in Article 2 (4) of the UN Charter and the exception of self-defence.\(^{36}\) It is submitted that

\begin{flushright}
32 Judgement of the International Military Tribunal at Nuremberg, 1946, 1 Trial of German Major War Criminals Before the International Military Tribunal 208 (1947).
35 Kunz, Josef L.: op. cit. 877.
36 Several authors maintain that such a general prohibition and the centralisation of the power to use force is a necessary
\end{flushright}
self-defence as defined by Article 51 is – besides a collective enforcement action authorized by the Security Council - the only exception to Article 2 (4), i.e. the wrongfulness of the breach of Article 2 (4) by unilateral use of force might be precluded only if it is in connection with an armed attack against a Member of the United Nations, and until the Security Council has taken measures necessary to maintain international peace and security. It goes without saying that other requirements established by customary law and left unmodified by the UN Charter, including necessity, proportionality and immediacy, also must be fulfilled. However, it is important to note that situations may occur when threat or use of force is not in violation of Article 2 (4) of the UN Charter. But in such cases the State using force inevitably infringes other obligations established by international law towards the State targeted by its actions. The wrongfulness of these acts might also be precluded by invoking Article 51 since if it serves as an excuse for breaches of Article 2 (4) then it certainly might preclude the wrongfulness of a less serious breach of law.

Even though Article 51 is the only exception to Article 2 (4) as regards the individual recourse to force, it is not the only circumstance precluding the wrongfulness of a conduct not prohibited by Article 2 (4) but illegal under other provisions of international law. Since the UN Charter contains no provisions as to these circumstances, such as the state of necessity, recourse have to be made to other sources of international law. It seems that the UN Charter created a two-fold system of circumstances precluding wrongfulness. Self-defence has been elevated to a higher status than that of other excuses previously recognized by general customary law but at the same time it was given a rather restricted meaning. Other circumstances precluding wrongfulness remained intact in substance but their scope has been confined to violations of obligations other than that of Article 2 (4) of the UN Charter. The question whether there exists a residual “right” of self-defence covering violations other than that of Article 2 (4) must be answered in the negative. The situations occasionally described by using the expression “self-defence” but not having the characteristics required by Article 51 might be in fact manifestations of other circumstances precluding wrongfulness, and should be judged accordingly. The reason for holding on to an ancient and expanded interpretation of self-defence is usually attributed to the fact that these other circumstances precluding wrongfulness historically evolved from the broad concept of self-defence, and there are authors according to whom there is no use of cutting the “umbilical cord.” However, the author of the present article cannot resist the temptation to quote in this regard the remarks of Roberto Ago stating that

the reason is largely that many of these writers remain wedded to notions and to a terminology – which this writer regards as incorrect – drawn from a relatively antiquated portion of State practice with which they are more familiar.

III. Self-Defence and State of Necessity Revisited

In the fight against international terrorism the most intrinsic problems of justification of the use of force and State responsibility under international law arise when a State has recourse to forcible measures in the territory of another State without its prior consent. Although a detailed analysis of consent as a circumstance precluding wrongfulness and its relation to the recognition of a

prerequisite for creating a legally meaningful definition of self-defence, see e.g. UN Doc. A/CN.4/318/Add.5-7, paras. 83-87. (report prepared by Roberto Ago). However, it is often asserted that self-defence might have a function in a legal system that does not object to the recourse to war, e.g. Waldock, C.H.M.: The Regulation of the Use of Force by Individual States in International Law. 81 RCADI (1952-II) p. 457.

37 For the notion of the differentiated character of peremptory norms (jus cogens) see: Commentary to Article 33 of the Draft Articles on State Responsibility, paras. 22-23. UN Doc. A/35/10, para. 34, 2. In: A/CN.4/SER.A/1980/Add.1 (Part 2)


39 UN Doc. A/CN.4/318/Add.5-7, para. 113.
government would exceed the limits of this study, it must be noted that military operations in Afghanistan were concluded against two closely linked but separate entities: the Taliban and the al-Qaeda network. The al-Qaeda is nothing more than an international terrorist organization which is not a subject but merely an object of international law.\textsuperscript{40} The Taliban is an insurrectional movement and therefore entitled to at least an insurgent status under international law, but until lately it might have been regarded as a \textit{de facto} government operating in 90 to 95\% of Afghanistan. At its peak it was formally recognized by three governments (Pakistan, Saudi-Arabia, UAE), but the United Nations and all the intervening powers were of the view that the legitimate government of Afghanistan is that of Burhanuddin Rabbani, consequently it alone has the right to represent the country in its international relations.\textsuperscript{41} There are no indications that the consent of the recognized government of Afghanistan was requested before the beginning of the military operations, and it seems obvious that the forcible measures would have been carried out even if the consent had been denied.

The UN Security Council has declared on several occasions that international terrorism in general\textsuperscript{42} and the situation in Afghanistan in particular\textsuperscript{43} constitutes a threat to international peace and security. However, this finding in itself has never been considered an authorization or a proper justification for the use of force in the territory of Afghanistan. Nevertheless an interesting novelty is presented by two Security Council resolutions\textsuperscript{44} adopted shortly after the terrorist attacks of 11 September 2001, i.e. the recognition and reaffirmation of the inherent right of individual or collective self-defence in accordance with the Charter. The precise meaning and legal consequences of this statement are far from being clear but it definitely signals a change of attitude as compared to the reaction of the Security Council to the embassy bombings in Nairobi, Kenya and Dar-es-Salaam, Tanzania that took place on 7 August 1998.\textsuperscript{45} The two relevant resolutions of the Security Council refrain from declaring the existence of a situation of self-defence in the particular case, and can by no means interpreted as the justification in advance of any coercive action taken in response by the United States and its allies. As far as the progressive development of international law is concerned these documents do no more than reiterate the view already shared by a significant segment of the international community that under certain conditions self-defence might be a circumstance precluding the wrongfulness of otherwise illegal measures taken by or with the approval of an injured State against entities involved in international terrorism.

It is commonly held that the situation of self-defence in international law occurs in interstate relations. During the codification process on the topic of State responsibility the UN International Law Commission (ILC) expressed its conviction that the State against which another State acts in self-defence is itself the cause of the threat to that other State. It was the first State which created the danger, and created it by conduct which is not only wrongful in international law but also constitutes the especially serious specific international offence of recourse to armed force in breach of the existing general prohibition on such recourse.\textsuperscript{46}

\textsuperscript{40} Of course it is not suggested that the application of the rules of war and of the Geneva Conventions is \textit{ipsa facta} excluded. The importance of this issue is highlighted by the recent treatment of al-Qaeda detainees in US custody. In this regard see: Hailbronner, Kay: \textit{International Terrorism and the Laws of War}. 25 German Yearbook of Int. Law (1982) 169.

\textsuperscript{41} Mr Rabbani has agreed to transfer power to an interim government established pursuant to the agreement concluded in Bonn-Petersberg on 5 December 2001. See: UN Doc. S/2001/1154.

\textsuperscript{42} E.g. S/RES/731 (1992) reaffirming the right of all States to protect their nationals from acts of international terrorism that constitute threats to international peace and security.

\textsuperscript{43} E.g. S/RES/1189 (1998). At that time the invocation of Article 51 by the US was not echoed by the Security Council. This point is made in: Stahn, Carsten: \textit{Security Council Resolutions 1368 (2001) and 1373 (2001): What They Say and What They Do Not Say}. www.ejil.org/forum_WTC

\textsuperscript{44} Commentary to Article 34 of the Draft Articles on State Responsibility, para. 3. UN Doc. A/35/10, para. 34, 2.
The same view is reinforced by the commentaries to the final version of the articles on State responsibility adopted by the International Law Commission on its 53rd session:

The essential effect of Article 21 is to preclude the wrongfulness of conduct of a State acting in self-defence vis-à-vis an attacking State.⁴⁷

Thus the invocation of self-defence is permitted only if an armed attack occurs by a State directed against another State. The acts of 11 September 2001 were apparently directed against a State since they aimed at the destruction inter alia of State or government facilities for which a useful definition is given in Article 1 of the International Convention for the Suppression of Terrorist Bombings.⁴⁸ Furthermore it seems appropriate to regard any act intended to cause death or serious bodily injury to a civilian, or to any other person not taking part in the hostilities in a situation of armed conflict as an attack against a State if the purpose of such act is to intimidate a population or to compel a government to do or to abstain from any act.⁴⁹ No problems of attributability emerge when such actions are perpetrated by organs or agents of a State. In this case, however, a paramilitary organization was involved for the acts of which a State can only be held responsible if the organization acted in fact on behalf of that State. The existence of a de facto State organ can be ascertained only if a State is shown to exert effective, overall and specific direction and control over its operations.⁵⁰

If this requirement is fulfilled it is the act of the de facto State organ itself which is to be examined whether it constitutes an armed attack. In absence of such organ it must be determined whether the assistance, falling short of direction and control, to the paramilitary group by a State in the form of the provision of weaponry or financial, logistical or other support amounts to an armed attack. The records of the San Francisco Conference contain no explanation of the term “armed attack.” In the traditional interstate warfare the meaning of the phrase would be sufficiently clear excluding sporadic operations by armed bands, border incidents and minor attacks that can be countered without military operations across frontiers.⁵¹ The scale and effects of the attacks of 11 September 2001 are comparable to that of a co-ordinated and general campaign of regular forces therefore clearly fall under the scope of the concept of armed attack. On the other hand the author is not able to determine whether it would be feasible to consider regularly recurring small-scale violent actions (e.g. fedayeen raids) as being part of an armed attack.⁵² However, based on the information at our disposal it would be highly inappropriate to regard the individuals participating in the attacks of 11 September 2001 or the al-Qaeda network itself as a de facto organ of the Taliban.

The situation is further complicated by the fact already referred to above that the Taliban received no general recognition as the legitimate government of Afghanistan. Therefore it remains unclear to what extent are applicable the rights and obligations of States established under international law in this particular case. It is a general principle of international law that every State has the duty to refrain from organizing, instigating, assisting or participating in terrorist acts in another State or acquiescing in organized activities within its territory directed towards the commission of such acts.⁵³ The Security Council has clearly extended this obligation to the Taliban although it is never referred to as a government of a State but merely a faction which also calls itself the Islamic

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⁴⁷ Commentary to Article 21, para. 5. UN Doc. A/56/10, para. 77.
⁴⁸ 37 ILM 251 (1998)
⁵¹ Brownlie, Ian: op. cit. pp. 278-279.
⁵² A view consistently held by Israel. See e.g.: Repertoire of the Practice of the Security Council 1975-80, p. 402; 1985-88, p. 429.
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The Emirate of Afghanistan and controls some areas of Afghanistan. The Taliban has obviously disregarded these orders which conduct might entail its responsibility under international law. In order to enforce the compliance with international obligations the recourse to lawful countermeasures is permitted. However, according to the present state of international law lawful reprisals might not involve the threat or use of force. Presuming that the concept of self-defence is applicable at all to acts committed by a “faction”, the wrongfulness of the use of force is precluded by a situation of self-defence only if the support provided by a “faction” to a terrorist group amounts to an armed attack.

Such support could easily be classified as an act of aggression following the definition annexed to General Assembly resolution 3314 (XXXIX). But the terms “aggression” and “armed attack” are not synonymous and were constructed for entirely different purposes. According to a convincing argument submitted by Bowett, the concept of “aggression” is an auxiliary instrument used by the Security Council and the General Assembly in determining whether a situation constitutes a threat to international peace and security. The expression “armed attack” is supposed to have a much more restricted meaning describing a situation where an individual State might have recourse to force against an aggressor State even without the prior authorization of the Security Council. The International Court of Justice has ruled that the concept of “armed attack” does not include assistance to rebels in the form of the provision of weapons or logistical or other support without being substantially involved in the operations thereof. Despite the Court’s unequivocal finding an opposite view seems to emerge due to the proliferation of State sponsored terrorism:

Obviously, it would go too far to say that the mere presence of terrorists in a State meant that the State was involved in their armed attacks, but when a government provides weapons, technical advice, transportation aid and encouragement on a substantial scale, it is not unreasonable to conclude that the armed attack is imputable to that government.

In addition some authors expressed their opinion that even if the conditions of an armed attack are satisfied,

the proportionality rule will usually not justify direct action against the supporting State, while it might allow attacks on the bases of such groups of foreign territory.

The outrage caused by the attacks of 11 September 2001 and the firm determination of the international community to take immediate and effective measures against international terrorism is certainly able to provide the necessary impetus for the expansion of the traditional concept of self-defence. The author, however, is convinced that a modern and adequate response to the legal challenges presented by the fight against cross-border terrorism can only be reached by the

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54 According to S/RES/1267 (1999) and S/RES/1333 (2000) the Taliban is called upon to cease the provision of sanctuary and training for international terrorists and their organizations, take appropriate effective measures to ensure that the territory under its control is not used for terrorist installations and camps, or for the preparation or organization of terrorist acts against other States or their citizens, and cooperate with efforts to bring indicted terrorists to justice.
The progressive development of the notion of *status necessitatis* as a circumstance precluding wrongfulness.\(^{59}\)

The International Court of Justice has strongly reaffirmed that the state of necessity is a ground recognized by customary international law for precluding the wrongfulness of an act not in conformity with an international obligation, and quoted with approval the basic conditions set forth in the ILC draft articles on State responsibility as reflecting customary international law.\(^{60}\) Accordingly, the state of necessity precludes the wrongfulness of an act otherwise illegal only if an essential interest of the State violating its international obligations is threatened by a grave and imminent peril not induced by the invoking State, and the acts challenged are the only means of safeguarding that interest without seriously impairing an essential interest of the State towards which the obligation existed.

It is undoubtedly an essential interest of a State to protect its population at home and its nationals abroad. For this reason the humanitarian intervention, i.e. military intervention in another territory to rescue citizens under threat is widely tolerated by international law.\(^{61}\) The question is whether a state of necessity might preclude the wrongfulness of military operations of a larger scale designed to destroy governmental or non-governmental facilities serving the purposes of international terrorism, to obtain custody of individuals engaged in terrorist acts, and to otherwise terminate the grave and imminent peril caused by such activities. Basically this argument was proposed by the United States concerning the cruise missile attacks against paramilitary training camps in Afghanistan and against a Sudanese pharmaceutical plant on 20 August 1998.\(^{62}\)

In his report, Mr Ago has already contemplated this point and concluded that

In any event, while one can certainly discern in the discussions arising out of such cases in the Security Council a dominant tendency towards an attitude of the greatest severity of all forms of action which in one way or another constitute assaults on the territorial sovereignty of States, one cannot draw any conclusions from them, either for or against the admissibility in the abstract of the plea of necessity in such cases. ... The task of deciding what that answer will be therefore rests with the various organs responsible for [the] interpretation [of the provisions of the Charter].\(^{63}\)

In the author’s opinion the international *opinio juris* has clearly consented to this kind of interpretation since the attacks of 11 September 2001. The author does not believe in the existence of an instant custom, but if this change will be lasting, consequently the legality of the use of force might be judged by the standards of a state of necessity. This would certainly put into a new perspective the ongoing debate over anticipatory self-defence, since the presence of a grave and imminent peril obviously does not require the actual occurrence of an attack. Furthermore there is no need to prove the wrongfulness of the State whose territory is being targeted.

On the other hand, the actions permissible in a state of necessity are much more restricted in scope and range as compared to self-defence. The sole objective of the forcible measures adopted in a

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59 The final version of the Commentary to Article 25 of the Draft Articles on State Responsibility (para. 20) also acknowledges that the rules relating to a state of necessity might have a role in this respect. *loc. cit. supra* note 28

60 Case concerning the Gabčíkovo-Nagymaros Project (Hungary v. Slovakia), Merits, 1997 ICJ Rep. 7 paras. 51-52.


62 Murphy, Sean D.: *Contemporary Practice of the United States Relating to International Law*. 93 AJIL (1999) 161. This has been the case even though the US invoked Article 51 of the UN Charter and tried to establish some fault on behalf of the Taliban and the Sudanese government. None of the targets were State or government facilities.

63 UN Doc. A/CN.4/318/Add.5-7, paras. 65-66.
state of necessity is to terminate an existing, clearly identifiable, grave and imminent peril to an essential interest of a State. This goal does not include retaliation and must be distinguished from any form of self-help since its purpose is not the enforcement of existing obligations. These ends are to be achieved by an intervention that is extremely limited in time and extent.64 It is definitely an illegitimate objective to replace a government, and even the targeting of State or government facilities is questionable since it might be justified only under the more strict conditions of self-defence.

IV. Conclusions

In the foregoing it was argued that according to the present state of international law the use of force against members and facilities of terrorist organizations might be justified by a state of necessity, and the wrongfulness of an action taken against State or government facilities might be precluded by a situation of self-defence if a terrorist organization operates as a de facto organ of that State or the support provided by that State otherwise amounts to an armed attack.

However, the author is also convinced that there exists a hierarchy between types of response to terrorism, and that “only after every effort has been made to deal with a terrorist attack by peaceful means should States resort to military action.”65 International law being a highly decentralized legal order, the proliferation of unilateral coercive measures would have very undesirable consequences. The intent of the framers of the UN Charter was to create a system of collective security where individual recourse to force is an exceptional and temporary phenomenon. As long as the United Nations in general, and the Security Council in particular is unable and unwilling to discharge its essential functions, international law can do no more than mitigate the effects of the unequal balance of forces in international relations. Unfortunately, it seems that in the present state of affairs the international community has nothing more to offer than it did at the time when Thucydides wrote the famous Melian dialogue:

[You know as well as we do that right, as the world goes is only in question between equals in power, while the strong do what they can and the weak suffer what they must.66

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EVOLUTION OF THE LEGAL STATUS OF THE HUNGARIAN NATIONAL BANK AND OF THE HUNGARIAN FINANCIAL SUPERVISORY AUTHORITY (PSZÁF) IN LIGHT OF EUROPEAN PROGRESS

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For the financial policymakers of the European continent affected by the fever of unification, it became obvious in the nineties of the last century that the EU needs to implement significant changes in the regulatory aspects of its financial administration in order to aspire after a significant role in world politics. However, this was only a political recognition of an opinion well developed in professional circles, according to which monetary union must necessarily be followed by the integration of the financial market. But while the main driving force of the establishment of EMU was rationality in the public finances, the transformation of the financial market was fought for and achieved by the financial sphere itself, offering a spectacular evidence for the feedback between the governing forces and governed. Although on May 1, 2004, Hungary attained full membership in the European Union, but even because of its export-led economy and its close connection to the financial market encompassing the world, our country could not afford to disregard the evolving events. Let us review the fundamental changes affecting the domestic financial sector and the capability of the affected institutions to adapt to such changes.

1. Major changes in the financial market of the Union

The currently existing system (EMU) has emerged as a result of major milestones marking the development of the European Monetary Union (Intra-European Payment Agreements, European Payment Union, Werner plan, Delors report, etc.) and ESCB, the European System of Central Banks embodying its organizational substance, as well as the ECB, the European Central Bank. ESCB, the supranational network consisting of various banks, the European Central Bank (ECB) and the national central banks was established on June 1, 1998. This jointly created system is simultaneously characterized by centralization and decentralization. It is centralized, because the ECB itself determines the European monetary policy, but at the same time, it is decentralized, since the governor/president of each national central bank has a membership in the Board of Governors, which has a central role in the direction of the ECB, thus, all of them participate in decision making. The ECB is a legal person, it is forbidden to request or accept any instructions, consequently, the national central banks – which constitute integral parts of the ESCB – are also independent in this capacity, they are required to implement the instructions received from ECB.

It is obvious that the establishment of the ECB greatly increased the independence of the national central banks in personal, institutional and budgetary aspect, and the maintenance of price stability became their major task. At national level, each country responded differently to the changed situation. In some countries, the references to monetary tasks have been completely eliminated from
the laws pertaining to central banks, in some others, only the performance of analyses is possible at national level. In France, the central bank is allowed to create financial provisions within certain limits regulated by the ECB. Some other countries’ national sensitivities do not allow their national banks to form integral parts of the joint monetary policy, for example Finland and Portugal have regulated their own central banks in such a way that the contribution of the central bank to the formation of the joint policy be unambiguously obvious. According to the German rules, nobody can give directions to the president of the central bank, if he/she is acting as a member of the Board of Governors of ENSB. An interesting exception is that in New Zealand, a contract is concluded between the president of the central bank and the government, which guarantees the extent of inflation, along with all its legal consequences.

Nowadays, the first steps of a much greater progress can be observed. The daily quantity of money circulating on the money markets of the world, the increasing number of market participants, the increasing risk posed by the failure of interconnected national economies and enterprises all support the necessity of change, which can be tackled at the following levels – at an institutional and norm-creative level of the European Union, and in a close connection with the latter, at the level of individual national inspectorates, concerning organizational and management issues as well as their legal statuses, and finally, as an issue concerning the realm of constitutional law, in the area of norm-creating powers provided for the above parties.

The participants of the European Summit held on June 15 and 16 in Cardiff observed the crisis phenomena emerging in the European financial market, and in order to determine the reasons of the problems and ensure recovery, the Council of Europe called upon the European Commission to prepare an action plan for the improvement of the single market of financial services. The Commission determined that the principal norms of financial regulation of the Union are generally satisfactory, but the legislative techniques have to be much more flexible and expedite in order to adapt the rules of supervision to the changing market situation. But in order to ensure this, the common “wholesale” market for the European Union must be established, which requires a fundamental correction of the institutional and legislative system of the European Union. The basis of the reform was the so-called Lámfalussy Report (February 15, 2001) published by the “Committee of the Wise Men” under the direction of the Belgian banker, Sándor Lámfalussy.

According to the report, the most significant obstacle to the common financial market is the inoperability of the regulatory activity, as well as the time-consuming nature of the co-decision procedure, which is an established practice of decision-making in the Union. The rules created seemed inflexible and indecisive, the most fundamental rules required for reliable and predictable operation were missing, just as the mutually unambiguous norms, standards. The European Commission is overloaded and slow and it tends to overcomplicate things, national implementation suffers delays, and the constant supervisory approaches contribute to the growth of problems, as well. In his position, a four-stage approach of the problem can lead to satisfactory results. In the first stage, the Commission submits the draft directive – or regulation – to the Council, after thorough and widespread consultation, which pieces of legislation only specify the basic principles and the implementation powers. At the second stage, it shall propose the establishment of two new organizations – the European Securities Committee and the Committee of European Securities Regulators. The ESC would generally have regulatory tasks – within the implementation powers delegated by the Council to the Commission, it would decide on the regulatory proposals submitted by the Council. The CESR is an independent consulting body, which has the national securities authorities as its members, and it has a consultative role regarding the preparation of rules at the second stage. At the third level, the CESR helps the process by preparing recommendation, guidelines and standards, and measures the supervisory practices. At the fourth stage, the Commission inspects the compliance with the Community law on behalf of the member states and it can apply sanctions in individual cases.
In light of the ideas, the commenced changes went beyond the area of securities the investigation of the extendability of the Lámfalussy procedure to other financial regulatory areas has started. As a result of this, a new committee without any legal predecessor has been created in the banking area, whereas in the field of insurance, and insurance committee has been created based on the so-called Insurance Conference. The committee to be established in the banking field will not only have the supervisory bodies as its members but also the European Central Bank and the central banks of member states, even if the central bank of a given country does not have a supervisory function, with the restriction that only the representatives of supervisory organizations will have the right to vote.

The national supervisory institutions will form an active part of the newly created single financial market. Since the establishments of the inspectorates has remained at a national level, there are significant differences with the appropriate institutions of individual countries. In some countries, the central bank has a supervisory function (Italy, Ireland), but the situation is quite different in Germany and in Belgium where the central bank acts in cooperation with a complementary organization with centralized powers. A particular controlling system supervised by the central bank can be found in Portugal, Greece, the Netherlands, and Spain. And finally, there is a so-called particular system characterizing Finland and France – in these countries, individual, specialized organizations have been established to supervise the various branches of the single market. Thus, in this case, the national legislators have to decide which way to follow and which institutional system to adopt domestically.

As a result of the decision, controlling bodies independent of the central bank have been created in such a way that the legislation has only given the central bank the controlling powers absolutely necessary for completing its tasks. With regard to the inspectorates, it is indubitable, that the future belongs to single inspectorates instead of specialized supervisory bodies. The reason for all this can possibly be found in the prevention of the so-called arbitration, the cross-border presence of the increasing number of market participants, and the presence of sector-neutral inspectorates interested in international cooperation.

Even the Union acts in realization of the latter – the issue of supervision will remain within national powers, respecting individual characteristics, but it expects and promotes harmonization. The major objective of ESCB in this context is the creation of a stable monetary market, within a centralized, Union-based supervisory system. According to the existing agreements, the ECB can be granted special supervisory powers and the supervision-level coordination of the area has been achieved within the framework of the Committee of European Banking Supervisors.

Concerning the legal status of supervisory bodies: due to influences from the Anglo-Saxon legal environment, the financial inspectorates as administrative institutions, such as PSZÁF, aspire after new titles as regulatory bodies. The major task of regulatory bodies is the correction of failures in the operation of the market, guarding the subsistence of the conditions for market operation, similar bodies can be find in the areas of market competition regulation, regulation of general business services, as well as that of the local public services. The most important question to be clarified in connection with the existence of a regulating authority is its own legal status. On one hand, it is a central administrative body, not completely under government control, but the extent and significance of its independence does not reach those of independent branches of power. In reality, we can speak of “autonomous structures” where administrative powers and operative guarantees interrupt the superstructures built on the logic of the regular civil servant system.

Last but not least, we should refer to the problems posed by the norm-creating powers provided for nearly every national financial supervisory body. Reviewing the international situation, two distinct systems can be recognized: the practice signified by the British FSA (Financial Services Authority)
and the Danish and Swedish practice implemented following its example, and the German (Bundesanstalt für Finanzdienstleistungsaufsicht) and the Austrian practice. The British-Danish system gives broad legislative powers to the supervisory bodies (e.g.: general rules necessary for consumer protection, protection of good business reputation, in the areas of professional training and operation, price stabilization, financial services, rules against money laundering), together with the corresponding organizational and norm-creating assurances. As opposed to this, on the other side, the norm-creating powers of the supervisory bodies only concern the extent of the supervision fee and the regulation of business.

Nevertheless, it is important to note that in each related British parliament dispute, the constitutionality and in general, the norm-creating powers of the FSA are questioned.

2. Issues concerning the legal status of the MNB and PSZÁF

**Future legal status of the central bank**

Although even among the most prominent representatives of economics, there are several persons who exhibit doubts regarding the independence of the central bank, on a legal positivist basis ("The central bank is a product of legislation, it is created by laws, consequently it could even be abolished by legislation. Therefore, its independence is questionable. Milton Freedman), nevertheless, upon analyzing the history of development of European institutions, one can declare based on principle that the central banks have achieved an unique level of independence, the significant guarantees of which are elaborated in detail. Their unquestionable autonomies are supported by economics and enforced by the basic principles of the union, and – although not uniformly – expected by the public.

Thus, the first and most important issue is the determination of the nature of its independence. The central bank is independent and in this capacity, it is guaranteed by laws at national and Pan-European level, and as a result of accession, its supranational character is even more emphasized, which will lead to the loss of jus cudandae monetae (state right of coinage) with is a part of state suzerainty. The independent, daily decisions belong to the reality of the central bank, for which the bank is responsible, therefore it has to reject each initiative from the state which would transfer to it any responsibility for tasks not within its powers.

Although the Central Bank Act guarantees the independence of the Hungarian National Bank (MNB) – it is not allowed to request and accept directions from any organization except for the ECB, the President of the MNB has only a reporting obligation to the Parliament – the act has no reference to the relationship with the Union, but it regulates the bank according to its present legal status, as a completely independent institution. It is indubitable that before EMU accession, at a national level, it has achieved such a degree of independence as few other constitutional bodies, nevertheless it cannot be disregarded that at an European level, its maneuvering capabilities will be greatly restricted at an European level. Its domestic autonomy will be unquestionable but as a part of ESCB, it will not have a great deal of opportunities for independent action, since these are greatly determined by the decisions of the ECB both with respect to the goals to be achieved and the means to be selected. Nowadays, its real legal status is primarily determined not by the Constitution and the applicable Central Bank Act but the agreements establishing the organizational framework of the Union. Accordingly, the modification of the text of the Central Bank Act will be necessary in the future, thus several part of the act will be untenable, for example “the MNB shall determine and implement monetary policy, it shall create and manage official foreign exchange and gold reserves, create payment and accounting, as well as securities accounting systems, it shall form its monetary policy and the instruments to enforce this policy independently within the framework of this act.” Of course, in the future, it will do all this as part of the ESCB and its independence will be restricted
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Another severe problem at the practical level, which needs clarification in connection to independence whether any decision connected to the premiums of high ranking officials of the central bank should be within the powers of the Finance Minister. Upon establishment of the ESCB, following the common rules set by the member countries not only the primary legal guarantees are indispensable, but any authority given to the national government in this question is contrary to the principle of the independent central bank, which would be suitable for influencing the decisions of the central bank within its own powers. It is clearly understandable that this is contrary to the requirements, therefore it needs to be amended in the future.

The institutional, personal and financial independence of the central bank is a necessary but not a sufficient condition of describing the conditions determining the institution. In order to create a full picture, the basics of the interrelationship between MNB and PSZÁF have to be clarified. A long debate in Hungary and abroad as well is whether to divide supervision between the MNB and the supervisory body or to create an even higher supervisory body, or several smaller ones. It is indubitable that the MNB, as the “bank of banks” has to perform inspection as well, since this is dictated by its fundamental interests. Various solutions have been found in the world in this regard, but fundamentally, three patterns can be distinguished. Bank supervision is either within the powers of the central bank (formerly the United Kingdom, Poland) or a ministry, central administrative body (Japan, Canada), or an administrative body with special powers, which is independent from both the government and the controlling factors of monetary policy (currently the British FSA, Scandinavian countries). Supporting arguments can be found for both the independent supervision and the money market supervision within the powers of the central bank – the synergy of information supports integration, smaller inflation, more effective monetary policy. However, the mutually exclusive presence of monetary and supervisory policy (as a supervisory authority, the MNB is adversely interested in fulfilling its “last refuge” function), the change of bankruptcies passing through more easily, decreased accountability seem to speak against monist ideas. According to some opinions, if the supervisory authority is integrated with the central bank, it could decrease the political pressure on PSZÁF, according to others, the greater the powers of the central bank, the greater the danger of political intervention. According to the practice in the Union, anti-inflationary policy is largely opposed to bank supervisory activities, which would weaken the price stabilizing activity of the ECB, considering this fact, the Union is not planning on establishing a central supervisory body, but leaves the latter within national powers. Not even the Maastricht Treaty refers to union-level controlling policy, and the EU governing bodies support the Europe-wide separation of the two tasks. Accordingly, even in Hungary, controlling financial institutions is basically within the powers of PSZÁF, and the Central Bank Act leaves it within the powers of the MNB to control the compliance with the regulations of the central bank as well as with the conditions of performing supplementary financial services. All of these create favorable conditions, therefore, this status should be maintained in the future.

Other issues are to be decided in the future, as well. According to the opinion of a previous president, the monetary council should be built on a rotational principle in the future. A political and not professional debate has been conducted recently, in the subject of the supervisory body, as well. It is clear that it existence is a matter of decision. In Hungary, the law enacted in 1924 recognized the supervisory body with respect to the central bank, such as the legal materials of several countries, e.g. the Dutch or the Finnish legal system. The Irish, Spanish or Swedish legal systems use the respective State Courts of Auditors to fulfill similar tasks, in Austria, the same tasks are performed by external auditors. In Hungary, Act No. XXIII. of 2002 created the new supervisory institution, the tasks of which had been previously performed by the State Court of Auditors. There are arguments to support both solutions and it is obvious that foreign examples can be quoted in both cases. The accession to monetary union has raised one single question, correctly determined by László Kelemen (Gazdaság és Jog, 2001/3): if the current situation becomes permanent, the powers
of the supervisory authority with respect to monetary policy shall be abolished following accession. However, this was already abolished by the amendment in 2003.

**The legal status of PSZÁF**

PSZÁF has exhibited the most dynamic development in the area of financial control, in the past 14 years. The present organizational frameworks have been formed after multiple reorganizations, until it has swallowed all state authorities within the same field, following the example of the British FSA. In connection with the newly created higher supervision, we should describe the issue of its independence, which can be detected primarily in two areas – firstly in its relationship with the Ministry of Finance, and in this context, within the legislative framework determining its activities, and secondly, in the area of modifications required by the ever more intensive regulatory role.

László György Asztalos analyzed the independence of PSZÁF using a practical and not a scientific approach. In his study (Asztalos, 2000), he draws the following fundamental conclusions:

- **Legal independence**
  i. e. within the frameworks set by its own legislative act, with its own enforcement organization and with its own legal personality;
- **Appropriate supervisory system**
  it is important of whom the independence of the supervisory body shall be established, this has to be absolutely clear, otherwise, some other parties may tend to “take it under their wings”;
- **Independent revenue source**
  which ensures the security necessary for autonomous operation and renders it independent of budget disputes, and interested in a well-functioning market;
- **Independent personnel policy**
  which prevents the hiring of unqualified personnel and help the selection of appropriate professionals;
- **Independent foreign policy**
  which makes it possible for the supervisory body to keep contacts with the supervised parties and the press on its own right.

In order to clarify the actual relationship between the PSZÁF and the Ministry of Finance, political journalism should be avoided and the pieces of legislation should be used as starting points. One of the most significant problems is that Act No. CXXIV of 1999 on PSZÁF applies mixed concepts, which is not the first occurrence in the legal practice of Hungary. While in its first section, it defines PSZÁF as a national body under the direction of the government, in its Section No. 1/A, the Minister of Finance acting on behalf of the government has only some supervisory powers. Not to mention the fact that in Subsection (1), Item c., the Minister of Finance is only entitled to controlling. (Naturally, the three concepts are highly different and the content as well as the instruments of the three different levels of authority differ widely, just as the rights and responsibilities of the directed/supervised/controlled body.) Pursuant to Section 8 Subsection (1) of Govt. Decree 140/2002 (VI.28.) on the activities and powers of the Minister of Finance, the Minister is responsible for the supervision of PSZÁF. A complete clarification of the problem is not conceivable within the frameworks of this act, but it could be a highly significant step of the current reform process in public administration.
Examining the issue of independence of the currently operating PSZÁF, we arrive at the following results. Legal independence within the frameworks of the law is satisfied to the maximum, the supervisory system is well established. All this is valid with the remark that the lack of clarity of basis administrative concepts prevents the formation of a transparent system. The supervisory body has its own sources of income, but according to others, the PSZÁF offers no tangible services for the fees received, it essentially ransoms the participants of the market. However, the supervision fee is connected more to the market regulatory function of PSZÁF, and it is a material basis representing and creating the common interest of the supervised organizations and PSZÁF, in a way that is economical and works prudently, and is incarnated in the monetary market creating profits. With respect to the independent personnel policy, the amendment of Govt. Decree 150/1998 (IX. 18.) on the transfer of civil servants into reserve status and the open publication of vacant civil servant position, in a way, which avoids even the minimum possibility of political pressure and interpreting the independence of the regulatory authorities of the future on the long term, e. g. no transfer from reserve status is possible to a regulatory authority.

With regard to the processes and initiatives connected to the financial markets of the European Union to be discussed later, in the future, it will be natural for the director of the supervisory body to express an opinion at an international level. Due to the unfolding of a Single European Financial Market, the leaders of the European supervisory bodies have to conduct such independent professional policies which has European-level, occasional or daily activity as its integral part. Since sooner or later, all of the governments so far have had conflicts with the acting PSZÁF director in power, some further reflections on the issue would be necessary. The director of the supervisory authority should resist the temptation to voice his/her opinion in any daily political issue, especially in international fora, and the domestic political leaders have to respect differing (occasionally not to flattering) professional opinions, which are nevertheless worth thinking about.

Another important question is raised by the future changes arising from the role as regulatory authority. Tamás M. Horváth has emphasized in his study (Horváth, Magyar Közigazgatás 2004/7), that PSZÁF as regulatory authority has to be independent of the government. I would wish to refine this statement, I would add the following modification: the actual operation of the inspectorate should be independent of party politics but it cannot be independent from the operation of the government. Nevertheless, it must be remembered that although there are some real guarantees ensuring the autonomy of the market regulatory activities of PSZÁF, essentially, it is still an administrative body operating under the direction of the government, just as set forth in the act providing for its establishment. Thus, fundamentally, PSZÁF is an administrative body engaged in market regulation, which can obtain the legitimacy of its independence in and from this sphere, not the least because the authorities of the European Union react aggressively to any governmental interaction distorting the market. Thus, the inspectorate has professional independence, but this is not contradicted by the fact that PSZÁF as an organ part of state administration is not independent of the operation of the state. Thus, the PSZÁF Act is correct in establishing that the acting Minister of Finance is indeed responsible for the proper operation of the supervisory body.

Just another important statement: although the issues concerning regulatory authorities are constantly under discussion, we should remember that we do all these in the absence of any legal and/or administrative foundation in Hungary. Thus, in complete agreement with Tamás M. Horváth, we have to state that it is indispensable to create such legislation in the future.
3. Issues concerning the norm-creating powers of the central bank and the PSZÁF

**Regulation of the President of MNB**

Apart from the latter, both the Government and the Parliament have a fundamental deficiency in a very important area. Section 32/D Subsection (4) of the Constitution authorizes the President of the central bank to issue regulations within his/her sphere of activity stipulated in a separate law, which may not be contrary to the law. Accordingly, the applicable central bank law continuously specifies the authorizations for issuing regulations by the president of the central bank, despite the fact that Act No. XI of 1987 on codification has reference to such authorization of the president of the central bank.

Within the previously described ESCB system, the ECB has a right to issue regulations, accordingly, among the current EMU member countries some national parliaments have given the authorization, others have refused it with respect to the right of central banks to issue regulations. The currently effective, contradictory Hungarian legislation is problematic for two reasons: one has to decide whether such authorization is to be awarded to the central bank or not – the central bank of the respective EU member country has to issue its own regulations. Thus, this question seems to be decided. However, a significantly greater danger for the application of laws is that the law serving as basis for the Hungarian legal source hierarchy does not know any legal source which is treated as reality by both the Constitution forming the fundament of the legal system and the law regulating the respective institution. Thus, the constitutionality of the whole Hungarian legal system is questioned, the activity of the president of the central bank will be hindered, and our EMU accession will be seriously endangered from its legal aspect. It is important to note that the draft of the new codification law submitted to the Parliament in 2003 would enact the legislation in question, but this is still in progress, thus sustaining constitutional legal insecurity.

A similarly serious problem is that Section 51/A Subsection (2) of the Codification Act still upholds the right of assent of the Minister of Justice with regard to the provisions of the central bank. However, a favorable side of this disadvantage is that this does not concern the missing regulation, which would be completely unacceptable from the aspect of the independence of the central bank. Accordingly the draft codification act waiting for acceptance only upholds a right of opinion for the Minister of Justice.

4. Issues concerning the norm-creating powers of PSZÁF

Upon the establishment of PSZÁF, the model of the Financial Services Authority in the United Kingdom was regarded as an example, not just because of its organization, but with regard to its norm-creating powers. Thus, in Hungarian practice, primarily after analyzing the various processes abroad, the view has taken hold that the daily activity of supervisory authorities is inconceivable in the absence of norm-creating powers. Taking the international progress in consideration, it is necessary for the PSZÁF to start its campaign sooner or later to get new authorizations – this campaign has already been opened by the recently departing president, Karolyn Sass. Despite this fact, the PSZÁF Act only provides for the norm implementation power of the authority in its Section 4, apart from this, only the right of opinion is acknowledged. According to László György Asztalos, the conditions of the Hungarian codification powers are the following:

- clearly determined and delegated norm-creating powers;
- exactly regulated procedural structure;
- internal and external collegiate control;
- right of cassation of the Ministry of Finance (Asztalos, 2002.).
Out of these requirements regarding basic principle, the opportunity for internal control has been created by the establishment of a Collegiate Council. However, with regard to the above, and the events of the recent period, it is necessary to note the following: The current legislative control narrows down the supervisory authorization of the Ministry of Finance to a highly narrow range, and according to a faction of the political elite, this is more than would be possible. It is important to note that after each government change in the past years, the elite coming to power had a virtually fatal conflict with the directors of PSZÁF nearly every time, which organization would be interested in increasing its independence not the least due to European developments. However, beyond domestic conditions, it is worth thinking about in what extent the norm-creating powers of national authorities are contrary to the single European financial market. As Asztalos has correctly commented, the widespread English norm-creating authorization stems partly from the different English legal traditions and the existing wide political consensus based on a similarly wide societal consensus. The situation in Hungary in the 14th year following the political changes does not promise a similarly well-established, relaxed political atmosphere. Taking the European situation in consideration, it is my opinion that independent and widespread norm-creating powers of national supervisory authorities would be contrary to the currently emerging single European monetary market. Despite this fact, it is not inconceivable that PSZÁF will attain norm-creating powers in some areas in the not to near future, but none of these will reach the width of powers provided to the British or the Danish authorities. But in order to achieve this, it is necessary for the participants of Hungarian financial governance to be capable of acting as equal parties – the Ministry of Finance should not “swallow” PSZÁF, and the PSZÁF should not regard the representative of the Ministry as if they were its enemies.

**Summary**

It is obvious, that significant changes in the regulation of both institutions can be expected in the period to come. The independence of the central bank will be gradually increased at a national level, which autonomy will be completed after EMU accession. Apart from this, one needs to anticipate the fact that due to the incomplete development of the monetary system, it may face some serious changes. According to some analysts, this could have various outcomes, it can bring about the complete and finalized power of the euro, which will exert serious pressure on presidents of central banks upon the establishment of the ECB and by the emergence of an equilibrium between the ECB member states and the community institutions.

When examining financial supervisory bodies, it can be stated that currently there are more than forty organizations with regulatory functions at an EU level, the activities and the mutual relationships of which organizations are still unclarified. In order to achieve a much more effective convergence and cooperation, the major task is to decrease the discrepancies at an European level. However, there are still some very serious tasks facing the PSZÁF:

- Based on the Lámfalussy procedure, the supervisory body can mainly undertake the role of experts in the preparation and implementation of legislation and rules of implementation.
- All this is primarily manifest in preparing studies and participating in expert committees.
- Supervision in the pre-decision procedures of the European Commission will have an important role.
- With respect to implementation, the participation in the so-called comitology committees will be possible, but the Ministry of Finance will have new roles mostly in the consultative committees (CESR) and the regulatory committees (ESC).
- The PSZÁF will have the logical role of representing the Hungarian financial sector and the interests of the market participants.
- An increased level of cooperation has to be formed as well with the Ministry of Finance and the Hungarian National Bank in order to achieve uniform representation of national interests.
All this can have the consequence that the significance of the PSZÁF will greatly increase and its independence will be a minimum requirement appearing in the guise of European requirements and surrounded by guarantees. This can significantly accelerate the codification of an act called for by Tamás M. Horváth, laying down the elementary conceptual requirements and guaranteeing rules of administrative regulatory bodies. This could bring about a permanent specification for the limits of the independence of PSZÁF, either as referred to in the study by Asztalos (the director of the supervisory body would be nominated by the head of state, and it would only have a reporting obligation to the Parliament) or as a public law possibility described by Tamás Sárközy (Sárközy, 2004) in other respect. According to this viewpoint, the transfer of some of our constitutional or constitutionally highly significant institutions to the head of state should be considered, thereby guaranteeing their independence and increasing the legitimacy of the head of state.

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WHICH DIRECTION TO TAKE HUNGARIAN ADMINISTRATION?

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After the change of the political system in 1989/1990, the magnetic needle of Hungarian state organization and legal system - not for the first time in the last thousand years, but hopefully for this time definitely - turned towards west, and the European Union became the determinate center of magnetic attraction. The Association Agreement with the European Communities and their member countries in 1991, the submission of our application for the entry into the European Union in 1994, the beginning of the Entry negotiations in 1998 and the conclusion of the Contract of Entry in 2003 made it clear that Hungarian state organization and administration as part of the previous should fit harmoniously into the structure and methodology of the administration of the European Union.

The aim of the present study is to give an outline, within narrow bounds available, of the two pillars of Hungarian administration-constitution and personnel-their challenges, the answers given and also to attempt to point out the main directions of the development of Hungarian administration. In short, the study will make an attempt to answer the question posed in the title.

1. The structural system of Hungarian administration

1.1. Starting points

The structural system of the administration of a given state is influenced by many circumstances. From these the following should be emphasized: the size of the state’s territory, geographical characteristics: population characteristics (number, geographical position, religion etc. of inhabitants), the nature of the social-economic order, state of development in the division of labour, the nature of political will and its presence in decisions on state level, historical traditions, technological development, the inner principles of administration. These are the traditional determinative factors of the structural system. This fact should be underlined since - in my point of view – there is one new, not traditional factor, that is the international cooperation which has a formative influence on the administration structures of member countries. A good example is the membership in the European Communities and the European Union, of which more later.

The examination of the above formative factors of the structural system of administration shows that the factors are not static but rather dynamic that is continuously changing. The logical consequence of this is that the structural system adapting to the circumstances is also changing. Even though we know quite well that administration is a bureaucratic organization, the ”biggest factory” of the society and does not adapt itself easily to the continuously changing circumstances. According to historical experience the pressure of change is especially strong when changing the social-economic order, let the change be peaceful or revolutionary.
The thousand years changes of Hungarian administration and its structural system prove well things mentioned above, but I have no opportunity to discuss it here. I only refer to the well-known fact that there was a change of political system in Hungary in 1989/1990: the Hungarian Republic became an effectively independent, democratic, constitutional state that has its own political values. With other words: the Soviet Union made a strong influence on Hungary, announced the unity of state power, built on one-party system, a strongly decentralized social and economic order, which was followed by a totally new social-economical order that was built upon a democracy, power division and multi-party system, strived for decentralization operating market economy. The political consequence of this process is that the magnetic attraction of the development of Hungary became Western-Europe again. One of the most important constitutional representation of the change of political system - from the point of view of the administration - was the declaration that the Hungarian Republic is an independent, democratic constitutional state which operates market economy.

In my present work – because of size – I will not go into details of defining these concepts and their contents, but I am going to label these constitutional supporting pillars’ requirements that have an effect on the Hungarian administration, specifically, on its structural system, as challenges.

1.2. Challenges

According to the above, the democratic constitutionality and the market economy are the most important factors that have the biggest effect on the Hungarian administration and the structural system, as challenges. As we know, in 2003. 16. April Hungary signed the Contract of Entry to the European Union. According to this, from 2004. 01. May, our country becomes a fully qualified member of a state community which does not (sometimes exceptionally) word legal directions for the administrative organizations of the member states, but that has demands. These demands can be valued as challenges but they are certainly not internal but external challenges.

Examine that what kind of demands these internal and external challenges did generate against the Hungarian administration, and what type of challenges does the Hungarian administration have to face to, especially its structural system.

a) Challenges that come from democratic constitutionality

The constitutional state based on the following principles according to the modern sense of the word: the priorities of laws and legality, the success of the power-division principle, the extensive assertion of human rights. Considering these the Hungarian administration – in my view – corresponds the demands of the democratic constitutional state only if it represents and asserts the following features and characteristics.

- Clear and well-arranged structure,
- Consistent and unambiguous division of the sphere of powers,
- Harmonious enforcement of centralization and decentralization principles between the central and territorial-local state organizations,
- Assertion of the municipality principle in territorial-local administration, with proper state supervision,
- Operating an administrative court of law, legally binding administrative decisions should be attacked at judiciary and accept them as universal,
- Services and citizen-centered administration including public duties one-but gradually increasing-part transferring into not administrative organizations.
b) Challenges that come from market economy

Market economy is based on free and fair competition and does not tolerate neither monopolies nor the strong interference of the state and its presence in economy. But at the same time the state points out the compasses of the competition and ensures that the losers can live in social security. In the light of this - in my opinion - the Hungarian administration corresponds the demands of the market economy only if it represents and asserts the following features and characteristics:
- expediency, efficiency, success,
- interests,
- instead of subordination and superordination (in some places) have co-ordination in public affairs,
- instead of commanding and interfering administration there should be service and citizen-centered administration in accordance with constitutional level,
- adaptability and flexibility, representations of new constitutional forms infiltration into the structure,
- racionality and stability,
- systematicality, scientific foundality and foresight, systematic approach,
- getting to know the foreign solutions and their adequate representation in Hungarian administration.

c) Challenges that come from the connection to the European Union

The expectations of the European Union towards Hungarian administration, as challenges, can be interpreted only in the context of the connection of Communities and the national administrations of the member states. In this sense, we must make it clear, that the European Union on organization level is a building of such supra-national institutions that has a strong, legally defined relationship with the member states and with the national institutions of the member states. The relationship between the EU-institutions working on central level and on local level of member states can be called supplement principle or expressed with the help of Lajos Lőrinc’s words, these can be featured by the ‘administrative duty division principle’. This means the followings: there is an administrative division of labour between the EU-institutions and the member states and their own institutions, which means that EU-institutions - closely cooperating with the member states - set the aims, prepare the cases that belong to their sphere of powers, make decisions in them and control the fulfillments, while the member states and their institutions - tightly cooperating with EU-institutions - carry out the decisions.

On the other hand, we must clarify that there is no such command in the primary sources of communal law, that would order rules for the state organizations of the member states and in it for the structure, operation and its members. Literature says that there is no administrative acquis. According to these – the European Union – does not maintain power immediately on the administration of member states but it is certain that it has an influence on them: the acquis communautarie namely by communal achievements, implicitly like communal law and firstly the Treaty of European Communities is an expressis verbis, too. This oblige them to ‘result duty’ named by the terminus-technicus of communal law. This ‘result duty’ indicates three assertion of requirements contently. Namely: the administration of member states has to be reliable, clear and democratic.

What do these terms mean? The followings. It is true that the member states can freely organize their administration without any external influence, so we cannot speak about administrative acquis. For the EU it is indifferent what kind of organizative solutions use the national administrations and what sort of methods do they use, the civil service they have, the main point is that administration
should work that it can carry out communal tasks correctly by reaching the interests of economical, social and political aims aimed by the EU. The emphasis is on the reaching of communal aims, realizing them so on the effective usage of acquis communautarie.

On the behalf of these, European Union firstly expects that the administrative organization system of member states should be reliable: communal direction should be built in the legal system in time, these directions should be used effectively by different governments, and they must make it possible the continuous controll of their observations and the arrangement of legal debates by the proper resources. Reliability has to include the different parts of effectiveness: accuracy, rapidity, dynamic tolerancy and the promotion of economic integration which is the most important aim of the EU.

On the other side the EU also expects that the administration of the member states should be clear: the governments, being in connection with the communal services, should be unambiguous, the levels of decisions and duties should be accurately fixed and defined and the different institution’s spheres should fit into each other correctly. There has not to be neither vacuum nor power overlap.

Finally: the EU expects that the national administrative system should work democratically. The requirements of democracy mean constitutionality, having respect for human rights and basic freedom, multi-party system, government by the people, the apoliticality of civil servants, stability of laws and the predictability of administration.

From this analysis it is evident that reliability, clearness the requirement of democracy comprehends the whole administration. That is why we need to tighten our optics. We should examine what kind of requirements are there in terms of the administrative systems of the member states. We can state that there are no directly compulsors directions apart from some exceptions. (so there is no administrative acquis). But is it a fact that in the administrative systems of the member states general signs can be shown according to the following points.

In the central administration every member states have developed their own governments which deal with European affairs but nowhere occured an independent European Ministry. The solutions of European affairs by member states on the level of central administration can be put into two blocks. Decentralized and centralized modells. The main point in decentralized modell is that some central supreme authorities have a department which only deals with communal affairs. In this case the main task - and the main problem - is the coordination. (Germany, Spain) In centralized modell there is a central government into which the supreme authorities send their delegates. This central government is the Ministry Office (France) or it is under the supervision of the Parliament. (United Kingdom)

On the territorial level of administration a common determinig factors are regionalism and the strenghtening of self-government, the significant reduction of middle-level units and the increase of its population. The main causes of the strenghtening of regionalism – as a social, economical and political process - literature indicates: outbreak of ethnic movements, effect of new social controlling systems, regional representation of interests and the harmonic regional politics of the European Communities.

In this turn I want to refer to the fact that regionalism can be seen as an attack that comes from down under against the constitutional state, against the integration made by the European Communities, which attacks from above the constitutional state. I can also say that the European nations live in a double pressure from the second half of the 20th century: live under the pressure of integration and regionalism. Integration demands from the constitutional state that it should transfer its souvereinity for supranational governments. The regionalism demands the decentralization of the constitutional state so it should not give central duties for subnational governments and regions.
This double progress will lead to the fact that the constitutional state - as a historical category - will cease to exist in Europe and it will give its place to a really united European nation that is not shattered by constitutional states.

Going back to the territorial administrations of below central level. It should be pointed out that we can see not only governments like self-government but there are public administrative governments subordinated to the central government. The passing of central power reached both types of administrative organizations. The result of this "the role of public administration under the central administration does not loose its importance though the increase of decentralization." But its operation shifted towards relativ autonomy.

Regarded to the local governments of administration the following general features can be emphasized:

- The self-governing administration in most times is polysemic but these levels can only be co-ordinated to each other,
- Self-governments make the local civil affairs in a broad sphere,
- In the activities of self-government the serving feature dominates and most of their works come true by the coordination of different services,
- The head of self-government is a corporation those members are chosen by the local population, and there is an official executive apparatus behind it,
- There is a strong borderline between the members and governments of self-government dealing with political and official affairs,
- Self-governments brake out from the national limits and build wide range of international connections.

After the survey of the central, territorial and local administrative organizations of the member states it can be seen that in the last decades the European integration..."brought along the harmony of organization systems of the member states (europanization, if you like) especially from the point of view of functionality and value orientation.

The 1997 Amsterdam Contract was a significant step towards a united European Administrative Space when it set the task of "the gradual realization of freedom, security and justice." The European Administrative Space theoretically means a harmonious central value synthesis of administrative organizations of the member states and the legal practice that is built upon. The central organizations of the European Union does not have deconcentrated organizations built in the member states. As central development we cannot speak about independent administrative law as a branch of law, does not mean that in the last 50 years there were no requirement formulated in connection with the administration and staff of member states. These can be called European administrative principles and values. They determine with basic features the organizational and operative principles of this gradually developing place, which is in the European Union one of the most important guarantee. Among these principles and values - reliability, clearness and the demand for democracy and common judicial institutions - there is a place for requirements for the workers of the member states which says that the staff of administration should be stable, predictable, competent, qualified, proffessionalist and impartial.

Taking these into consideration the European Administrative Space - the administrative integration that is gradually done in the European Union - the main features can be selected as:

- Political development (democratic constitutional state),
- Economical development (social market economy),
- The reduction of national representative organizations, the strengthening of administration,
- The enforcement of decentralization, subsidiarity, solidarity principle, and as a consequence of these the strengthening of subnational and supranational organizations on the side of
constitutionality, on the other hand significant efforts for the reduction of differencies among regions on the behalf of gradual equalization,

- Reliable, clear and democratic administration,
- Field of actions that insure the reaching of communal aims,
- Mutual approach of different organization styles,
- Stable, predictable, competent, qualified, proffessionist and impartial departments.

1.3. Answers

Since the change of political system in Hungary the administrative system has changed a lot. These changes did not effect the central organization but the territorial and local organizations. I can simply say that, in the last ten years the updating of administration was meant by the reconstruction of the organization system and in it the territorial and local structures. It is not a criticism, but a fact. This fact was a natural consequence of the change of political system. These changes were the followings:

- In the life of the state the role of the prime minister and the government increased. The Hungarian government really governs. The executive power-as an independent branch prepares the laws and looks after the execution. It coordinates the supreme authorities, insures the local governments to be legally controlled. The constitutional situation of the prime minister gets stronger. The Parliament depends on him and also the functions and dismiss of ministers are in his hand.

- Cabinet system appeared as the new operating form of the Parliament. The Cabinet consists of the members of the Parliament which prepares the decisions of the Parliament.

- As a new legal institution - coming from the coa litic form of Parliament - appered ministers without portfolio.

- There was a small change in the structure of ministry and in the organizations that have a sphere of power within the country.

- The role of the Ministry Office is overestimated especially in 1998. The MEH is lead by the prime minister, it promotes the self-government interests.

- The structure of territorial and local administration have changed a lot, the council was followed by self-governments, so in the place of council system came self-government system.

- Local governments established their different alliances of interests, by breaking the common interests up and prevent the assertion against the central power.

- As a new and regional organization the Republic Legal Institution was established but it disappeared within a few years, it was followed by the County Administrative Office as a part of organization of the Parliament.

- In the countries—without any cooperation and conceptions—the territorial organizations of the central administration were founded, these were the deconcentrated organizations.

- Some administrative tasks were shifted into non-administrative organizations.

- The Police was a bit cleared, not tightly the security forces were built into the self-governments.

1.4. Problems and suggestions

The Hungarian administration reacted well and gave adequate answers to the challenges mentioned above referring to the main tendencies. I think we are quite far from saying that: the Hungarian administration is in the forefront of the world and solves its problems well. So there are problems and tasks deriving from it which can be summarized by the followings:

(1) It would be timely and justified to simplify and change the structure of the supreme authority of the administration ministerial and non-ministerial central administrative organizations.
In my opinion, the present structure is excessively divided and on an anachronistic way it suits the requirements of the socialist social leadership and it is adjusts to it even today. With regard to our connecting to the European Union it would be justified to simplify the Hungarian structure of supreme authority considering the inner division of communal law. That would be necessary that our country’s interests are asserted in the starting stage of making a decision by the central power. In this case one supreme authority can be responsible for regional and cohesional politics, and for the regional developments. It is good to consider because the European Union separated 2.847,2 millions plus 534,4 millions Euros for Hungary for the years 2004, 2005 and 2006, which we should utilize.

With the simplification of the structures of the central organizations most of the tasks and resources should be decentralized on behalf of the self-governing regions. It should also be considered that with the institutions of the European Union especially with the European Committee the supreme authorities should be in everyday connection and this is going to be their tasks. This means a meaningful extra work: we should take part in the preparation of laws and we should assert our national interests.

Speaking about the EU connecting and the labour increasement derives from it, the following quotation really reflects this increasement: "The size of the new task can be demonstrated through the example of Belgian administration, that they had to take part in 2580 sessions of 170 union workteam in 1994. During this time the Cabinet held 125 sessions, the COREPER (the community of the ambassador of the member states) held a session of 117. This kind of labour increasement that is waiting for the supreme authorities and for the prime ministers is a very important circumstance because on these levels will decided how we are able to assert our interests on the level of the union. So we should be really well prepared to these tasks and the ministry apparatus should also be prepared. This can only be successful if the discharge of ministries take place: if they get rid of the arrangement of official affairs. I think that in Hungary the supreme authorities have to deal with only three tasks group. (1.) the division and assertion of strategic directions of sectoral-politics, (2.) beginning of laws, preparation and law making, (3.) interests of Hungary and the assertion of national interests on communal level. For these it is very much needed, that the state reform asserting real decentralization should be carried out. There should also be an administrative and regional reform as a part of the state reform, but I am going to analyse it later.

(2) The place and role of the mid-level should be rethought in the organizing system of administration.

The number of administrative branches that are in the countries (country administrative office, country self-government, country territorial developing office and more than 30 deconcentrates branches) are too much, and their activities are not coordinated. In the end: the country level is disintegrated, so the country does not have a real ‘owner’. Especially the number of deconcentrated organizations, that are without any conceptions, are too much and their mere presence endanger the making of administrative tasks. The local communal affairs are also endangered. Imre Verebélyi wrote about this the followings in 1995:” In the last years a maximal possibly state was about to develop not a minimal needed (in the spheres of state deconcentrated organizations) while the possible independent self-government did not get any confirmation. ” In spite of the opposing reports we must say that: deconcentrated organizations do not carry out the principle of decentralization on mid-level but the principle of centralization. If we say that the country self-governments with a real legitimacy in the first place without any financial resources cannot be the real owner of the country, it becomes clear that there is a contradiction on country level between the communal law and the real functions of owners which cannot go on. It cannot go on because this situation goes at the expense of administration which is bureaucratic and in some cases the division of task and sphere of powers are not clear…This situation is not in harmony with the principles of European Charta of local governments especially with the subsidiarity principle.”
The question of regions should be mentioned. In my view, the simple clashing of countries into each other and these planning-statistical regions assert the interests of central powers instead of asserting the mid-level of a given region. Seemingly they carry out the principle of decentralization but in fact they assert the principle of centralization.

It is worth examining the opinion of a foreigner. He says the followings: "Hungary with its 19 countries and its 22 county towns and with Budapest, altogether 42 regional types of sphere of powers...does not stepped across the threshold into modern regionalism which fits into the requirements of European regional politics. The 7 regions of central administration and the plan of central administration can suit the minimum requirements of the European Union, they does not construct a suitable structure..."

I think it would be justified to cease the disintegration, and it would be needed to balance the centralization and decentralization principles on mid-level. This can be done by two ways, in my opinion: by integration and decentralization. I think that there is a new entity that has a corporation chosen by the population, and the mid-level organizations and their tasks should be integrated and the central tasks and resources should be decentralized. As Imre Verebélyi writes: "Between the central and territorial level just one mid-level is needed, and this should be work as a chosen level. The sphere of powers of this mid-level should be strengthened by the rearrangement of ministerial, administrative and deconcentrated sphere of powers. These regions can satisfy not only the needs of Hungarian administration but the requirements of European Union dealing with common resources and executions.

It is a hard question how many regions do we need. I do not agree with Imre Verebélyi who says that there should be a self-governing mid-level of 13-14 units that are built upon the present countries. I also do not agree with the leader of IDEA, Attila Ágh’s point of view who says there should be 7 self-government type of regions working simultaneously with the regional governments. Opposed to these views it is imaginable and I think it is really needed if there would be only 4 regions that can compensate the central power. These regions are: Dunántúl, Duna-Tisza köze, Tiszántúl and Budapest and its agglomeration. This opinion is based on the numerical conclusions that can be discounted from the solutions asserted in Europe. And based on that with the help of informational, communicational and new technologies it is easy to do the administrative tasks in the regional system.

Apart from the above I would like to clarify two things. One of it is that because of Hungary’s small territory, unitarian state system and historical traditions just one mid-level is needed in real. It is unnecessary to have a country level because the regions have their own legal, economical and intelectual sectors. The other thing is that we should accomplish the reform of the mid-level and the reform of the administration if we do not connect to the European Union. The connection gives only further impulses that are needed for further steps. The European Union does not oblige because it cannot oblige Hungary to change the administrative system. That is a different question that in the time of the EU connection it will be compulsory for us to have a communal law and the effective use of acquis communautaire which in my opinion can be done by the reform of territorial-level.

I know that the making of these reforms need social agreement especially the agreement of political parties becaus we should modify many laws even our Constitution. The reaching of social and political consensus is not the topic of this present essay and not the task of the writer. The question of small territories belongs to the problems of mid-level but because of content I will speak about it later.

(3) The state supervision of local governments’ work is not solved
The local administrative governments’ controlling sphere of powers does not replace the legal institution of state supervision. Literature calls attention here and values: ” with the expection of orders the controll moves in a limited place. It does not examine what is important. Because of the
deficiencies of state supervision’s task system... and because of the dragging on of the Constitutional Court and proceedings the effectivity of legal control is quite low and slow in spite the clerk’s work. I think it is high time that the local governments legal control should be changed by state intervention’s legal institution.

I emphasize it here that I think the effective state control of governments’ economy has to be solved as soon as possible. Literature has said for a long time that ”the economical and financial decisions of governments is missing and it is not solved its regular supervision. Including different people who claim different assistances.” Despite these warnings there were no changes in the past years. In consequence of these a great amount of governmental money went away from the sphere of governments, not illegally but ethically in an objectionable way.

In one sense the clerks have a great power on the governments because they ensure the legacy of the works of the governments, and not only from outside but from inside, too. They work not only subsequently but previously. The works of clerks raise as many questions as answers as the control of governmental administration. The main problem is that according to the law the clerk belongs to the government but according to his duties he belongs to the state. This duality prevents the clerks in a balanced fulfilling of his work, because the government expects him not to make difficulties and he should find the best legal solutions for the government while there is no such solution. I think the solution can only be if this duality is ceased to exist by making the work of clerks independent. He should be the member of the state: he separate from the law of labour or at last his appointment and relief should be tight to the opinion of the leader of the administrative office.

(4) The weak mid-level of the governments, the territorial system of self-governments which ahas a disintegrated structure arrived to the end of financial and economical productivity. Its possibilities and resources got exhausted.

The law of LXV. in 1990. about the local governments – contradicting to European tendencies and rationalities - allowed to every settlements to have a self-government. During the change of the political system it was quite understandable and it could be interpreted so it was not a surprise that the settlement-governments doubled compared to the councils. Today its number is more that 3000 and is gradually growing. This endangers the unity of Hungarian administration, and life proved the uncapability of living of small governments. (like schools, nurseries ect.). It seems that by declaring the freedom of governments and making circle-clerks is not enough to solve the problems and a strong state intervention is about to come. It would be really necessary to wake up from the intoxication of the change of political system after more than ten years. (I would like to mention it in brackets that together with the territorial reform and with strong state intervention the number of self-governments was lowered in most states of Western Europe like in Sweden, Germany and in Denmark in 1960 and 1970. The reduction was about 50%). From the governmental reforms of Western European states we can draw two morals. One is that as a result of merging local governments, a small number of ”strong” local governments have been created that require a ”weak” medium level (Swedish model) On the other hand the great number of ”weak” local governments in small villages require a ”strong” medium level and they also require a strong interest in association (French model). Both models are workable, both of them can be either good or bas, so neither of them have value in themselves. However, it makes you think deeply that in Hungary the reform of local governments resulting in the number of civil service organizations being doubled started when the reform of the opposite direction in Western Europe had already been over. I ask a question under my breath, quoting László Kiss: ”Is it possible that the development will not justify us?”

It also makes you think that in Hungary the great number of local governments require a ”weak” medium level and a mild interest in association. This is neither of the two models implemented in Western Europe, it is an unfortunate halving of them. (I ask again: ”Is it possible that the
development will not justify us?" and I answer it: Definitely not!) The consequence of all this is that our present system of local governments is not workable, as the practical experience show this as well. The government and the lawmakers must decide and be consequent in the following:

a) If the current system keeps going, a differentiated installment of tasks and scopes should be done. A strong medium-level local government organization and a strong interest in association should be created.

b) But if we want to keep the weak medium-level local government organization, a powerful merging of city and village organizations is necessary besides the installment of differentiated tasks and scope.

However, in both cases the financing of performing tasks should be reformed. This is essential to the implementation of a successful organizational and operational reform. If we do not make this step, we can say "in five years we will be at a stage where we were ten years ago".

The matter of small regions is closely related to that of the local governments because specific regional developing and civil service tasks are carried out by a number of geographically defined circle of local governments as per the law. The small regions do not have the right of self-governing, neither the autonomy attributed to local governments. In my opinion this the organization of small regions is necessary only if the state or the lawmakers decide to stay with the disintegrated structure of local governments. In that case there are and there will be tasks that the little villages will not be able to perform on their own because of their limited abilities and opportunities. If the disintegrated structure is going to be transformed onto level of cities and villages, a structure of local governments would be created that would be small in number but these organizations would have big and relevant financial and mental resources regarding their area and population. These local governments would include the cities and the neighboring villages in themselves. Thus the current system of small regions would be "solved" in this new system. The organizational activity between the cities and villages of the small regions would stop and it would be transformed into autonomy.

I regard the above description as the future scene of the Hungarian system of local governments. This structure would really decentralize balance the central government. This regional structure would have four parts. This structure would be complemented by the strong system of local governments consisting cities and their neighborhoods with relevant areas, population and resources. Thus a simple and clearly visible system would be created where the tasks scopes are shared and the tasks can be effectively performed. The result would be a system with transformed structure: central authorities with different structures and tasks, regional local governments and city governments. It can be seen that I more or less agree with Ernő Szigeti that "in the far future it is possible that the number of local governments will be greatly decreased, a system based on cities and their neighborhoods, which would cause the establishment of a regional level instead of the counties." My agreement is not complete with the above statement because I consider this reform realizable in the next 3 to 5 years.

(5) The fastness of handing over the civil service tasks to civil organizations and to so-called indirect civil organizations (public bodies, foundations, public utility companies, professional self-governing bodies, other economic companies) is not powerful enough.

The pre-requisite of this handing over would be a strong civil and entrepreneurial stratum and the establishment and strengthening of civil organizations. The matter of the fact is if the political parties, which hold the power, really want to hand over the tasks of the state, whether they want the civil service tasks to be performed by subjects who follow the civil law. At the time of the political changes and then later before the elections the parties often talked about the concept of “small state – cheap state”. Unfortunately this concept has remained an empty phrase so far. This is really painful if we look at how the developed states have already handed over their tasks to the indirect
civil service organizations and how much experience they have gathered by now. Their experience is positive: the tasks can be performed more effectively, faster and cheaper and with those who are involved in the matters. These organization are flexible, they have more freedom in handling the budget, selecting and paying their employees. They are more solvent and have taxation advantages and can perform the tasks free of politics. At the same time the traditional way of performing public tasks has its own advantages: possessing the needed information, the procedures strictly follow the rules, they are clear and reliable. There is a chance for recourse and for the protection of rights as well as the control of the parliament. István Balázs comments: "It would be a mistake to believe that the methods and forms of private civil service represent value in themselves… basically the indirect civil service is not an alternative to the hierarchical civil service, nor to the local governments. It rather increases the freedom of motion."

I should raise the question here which public tasks should be given to the indirect civil service. The international practice shows that the most appropriate tasks for the indirect organizations are the following: at the central level it is the management of the press and media, environment protection, energy and minority policy, at the local level it is the cultural and education matters, consumer protection and the supervision of the market. Today, the civil organizations take a much smaller part in the decision-making mechanism of the government as Lajos Ficzere comments. In a democratic state the citizens should not be only subject to the governmental decisions but they also need to take part in them actively.

(6) In the Hungarian civil service we can scarcely find or in some cases we cannot find those requirements that are evident in the developed countries and in the Hungarian economy nowadays. These are: quality, quality control, performance, evaluation of performance, efficiency, concern. My viewpoint is that the enforcement of these requirements is not contrary to lawfulness as shown by the examples of developed countries. In the past decade the victory of the political changes made it reasonable to put emphasis on lawfulness instead of the above requirements. The primary task was establishing and strengthening the democratic institutions and their lawful operation. Today these institutions have already strengthened and we need to re-evaluate the relationship between lawfulness and efficiency. It is difficult for both criteria to be in effect at the same time, so we cannot avoid the hard task of working out compromises.

The point here is what Henry Fayol expressed briefly over a hundred years ago: “the civil service can be industrialized.” Károly Martonffy also wrote: “all those methods and principles that the moving and inventive commercial and industrial spirit had created can be without exception applied to the operation of man’s moral organizations as well. “ A reasonable amount of experience has been accumulated on this subject in the developed countries, first in the area of budget planning then in other sections of community life.

(7) The internal organizational structures of the civil service are inflexible, different organizations often copy each other. The decision-makers apply the new organizational-structural solutions (matrix organizations, divisions, ad hoc work groups) of the developed countries and economy only in rare cases. They do not really know the practice of adequate and quick answers to the raised questions, thus they cannot adapt to the environment. We should not forget Charles Darwin’s words: in the nature it is not the strongest, nor the biggest, nor the most intelligent race survived, but those ones that were able to adapt to the environment. One barrier to adapt can be the characteristics of bureaucracy e.g. reliability as a value. Reliability, working according to rules and the hierarchy are basic requirements for the civil service. These elements each and altogether result in the inflexibility of the system.
In the past years the organizational system of the civil service was dependent upon persons, it was too sensitive to politics. The central politics strongly determined the system of civil service (central control of employment, industry and commerce), the professional and scientific considerations were ignored. It would be reasonable to build guarantees in the constitution to stop these adverse tendencies. It would be advisable to adopt the practices of developed countries where the political parties do not generally change the structure of the civil service.

There are historical and professional reasons that show the necessity of restoring the independent civil service court. The historical reasons are: until 1949 in Hungary there was an organizationally independent court which was separated from the ordinary courts and it had its own code. The professional reasons: Here I mention two excellent authors because I think they used the most appropriate wording. Lajos Lőrincz: “the decision which eliminated the independent civil service court gave the ordinary judges the right to inspect cases and it ignored basic reasons for incompatibility. First of all, the decision ignored the fact that the ordinary courts operate in countries where there are not separate courts, there is not civil service law.” András Patyi finds a similar result but different wording: “Our current system is based on out-of-date principles it is non-constitutional, its organizational solutions are thoughtless, careless, they ignore any principle considerations, we cannot see clearly, the system wears its own civil law, civil service features ashamed. I think the restoration of the independent civil service court could be connected to the re-regulation of the scope of the Constitutional Court.

2. The personnel of the Hungarian civil service

There is a standpoint in the Hungarian literature of law which says: “the civil service is the activity of a definite number of public servants in such organizations which represent the community, the state.” This definition identifies the civil service as a definite number of employees and their activity. This shows the importance of the personnel in the civil service well. The practical experience shows that the quality of the civil service performance and the satisfaction of the population basically depend on how fast and how well the public servant carries out the cases, how they behave, how qualified they are and also how moral they are.

In my opinion the legal relationship of public service cannot be identified with the fact of working in the civil service, with being a public servant. As the latter one is a narrower concept, and is only one element of the legal relationship of public service. I think the public service is a legal relationship between the state and the citizens with the purpose of working, including justice employees, attorneys, civil servants and also the professional members of the armed forces.

What are the specific features of the civil service legal relationship? The civil servant:
- does a state job,
- is employed by an organization that represents the executive power (public administration, local government) or at the Parliament, Constitutional Court, at the office of the President or a parliamentary delegate or works for the State Audit Office or the Economic Competition Office,
- exercises public power,
- is basically involved in law preparation and law enforcement activities. This needs to be codified in separate laws regarding its content and form and needs to be empowered with further special rights and duties.

As far as I am concerned, based on these criteria the public servants can be easily and clearly distinguished from any other state employees. The number of people on staff is often in question regarding the public servants. On one hand, which factors determine their number, on the other
hand, whether their number is high or low compared to that of other countries. It is very difficult to give clear answers to these questions, it is often impossible. Each country uses different terms to designate the same group of employees. So only similar categories can be compared regarding these questions. (Some states regard the members of armed forces and the employees of other public institutions as public servants.)

In the professional literature there is an agreement that the extent of the state’s role and the rate of the state jobs and also the standard of living are important factors in the number of public servants. One defining factor is the number of population, so those people who need the service of the civil service. Actually the most important factor is the rate of public servants and the overall number of employees. However, we cannot deduce clear consequences from these data, as the concepts on state jobs vary from state to state.

In Hungary the rate of employees working in the public service is 21.6% while it is 24% in the European Union. Regarding the number of public servants, I need to refer to the fact that some leaders of some states decide to reduce their number from time to time, but these intentions do usually not result in success. The reason for this is not only the characteristics of bureaucracy, but also are the following facts: the public servants are the main supporters of the state leaders, so the leaders are not really interested in weakening this group, on the other hand the public service tasks generally grow in number or they become more complex. These tendencies mentioned above could be experienced in the past years in Hungary, so the politics must take them into account in the future. The experience of developed states shows that the best way of direct savings in cost is not the decrease of the number of civil servants.

2.2. Challenges, requirements expected from public servants

In the democratic states the rights of public servants are strongly counterbalanced by obligations stated in several laws. The general obligations in the EU are the following:
- loyalty to the constitution and the state,
- impartial and reasonable procedures,
- strong limitation of other jobs that could be done beside public service, strict rules of incompatibility,
- obligation to give information and keep secrets,
- fulfilling the service obligations, obedience,
- unity of ethical and legal responsibility.

These obligations come from the legal principles of civil service and public service, which were developed from the judgment practice of the European Court. The sentences of the European Court form a source of the EU legal practice, so the member states are obliged to enforce the principles in their public service. What are these principles?

a) reliability, predictability
b) openness and transparency,
c) responsibility,
d) efficiency and serviceability.

In Hungary the political changes had a huge impact on public servants and their legal relationship as well. A totally new regulation was made (Law XXIII of 1992) and it opened a way to the development of a reliable, career-type, politically neutral and professionally qualified staff of public servants. The public servants exercise special rights, at the same time they have to meet special requirements. These requirements are listed in the preamble of the law as principles and are covered in detail in the various paragraphs.
The purpose of the law is to establish a public servant staff that can carry out matters independently of politics, lawfully and with up to date professional skills. These principles greatly cover those indicated in the developed countries and the EU. These principles are taken up in different paragraphs of the law:

- incompatibility of public servants and local government representatives,
- public servants need permission to have other jobs, also having other jobs in the case of senior servants is totally excluded, however the law allows them to do scientific, art, lecturing and editing activities,
- impartial handling of public affairs, public servants are forbidden to do jobs that are beneath them or jobs that endanger their impartial activity,
- a public servant cannot have active posts in any political parties, but they can be nominated by parties at the time of elections,
- public servants have to take a public service basic exam and also a special exam,
- the law also covers the system of obligations: on one hand the obligations are regulated as per the Labor Code, on the other hand the law defines the special requirements for public servants.
- public servants must carry out their duties according to the decisions of the leading boards, impartially and justly,
- public servants must keep state and service secrets,
- public servants must carry out their superiors’ orders,
- the law also regulates the public servants’ responsibility regarding constitutional, labor, civil and criminal law.

2.3 Problems and suggestions

(1) Professional requirements: my definite standpoint is that these requirements have importance not only in their application, but also during the public servants’ whole career as well. The development of professional knowledge is only implicit in the law. The qualifications are determined from only one side.

(2) The establishment of public service relationship or selection: Earlier I emphasized that the matter of personnel has a defining role in the public service, but the crucial point is the selection of public servants, in other words who is “let in” the public service. From this point of view the current regulation contains considerable problems:

a) there is not a central, government organization that would uniformly represent the state as the largest employer of the country,
b) the recruitment, which has been an ignored way of selection so far, should be made more intensive, varied and active in order to improve the quality of civil service,
c) the criteria of selection should be refined,
d) some preferences (minority, health) are totally missing.

(3) The system of qualification and its procedure: the evaluation of professional knowledge and skills is mandatory part of qualification, but the law does not establish the guarantees of gaining up to date professional knowledge.

(4) The matter of obligations coming from the specific public service relationship is not clearly laid out either. The greatest merit of the law is that is establishes a predictable way of promotion for the public servants. However, I cannot hide my fear that it also gives advantages to the “mediocre” because public servants can get promoted even if they just work a little. The point is that they must not make a serious mistake. The promotion is practically irreversible and this system puts the public servants “in concrete”, it does not give way to the excellent performance and does not encourage them to perform outstandingly.
(6) In Hungary the mandatory of evaluating the public servants’ performance was introduced too late, in 2001. There are concepts that sound strange in the field of public service even nowadays, while they have been known in the private sector for decades. E.g. quality, performance (efficiency, effectiveness, economy), the measurement of quality and performance. The international experts consider the efficiency of the civil service of basic importance in updating it. To increase the efficiency and competitiveness of the civil service we need to adopt the successful market methods from the private labor sector.

(7) Finally, I must state that the most important component of the civil service is the personnel. The quality and performance of the civil service greatly depends on the attitude and qualifications of the public servants. The lawmaker should provide stable regulation that would solve the problems mentioned above. The law has been modified 18 times in the past ten years!

Final Thoughts

The execution of the updating directions laid out above requires a systematic approach. It is high time to adapt the entire Hungarian civil service to the new circumstances. Also, the strongly centralized state power should be reorganized. So this is not just a simple reform of the civil service, but it should be the reform of the state. The other two branches must not be left out either: the courts that often make their decisions slowly and without any legal basis, and also the Parliament, which has too many representatives and it is totally disconnected from those who elected them. Hungary is being forced to step forward now. It is time for Hungary to carry out a reform of the state and a reform of the civil service in order to be a successful member of the EU.
JURISDICTION RATIONE PERSONAE IN ICSID\(^1\) ARBITRATION

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Field of research: Jurisdiction in ICSID arbitration

1. About ICSID jurisdiction in general

The purpose of this article is to clarify the issue of ratione personae jurisdiction in ICSID arbitration. Besides the two other jurisdictional requirements, i.e. written consent of the parties to submit legal disputes to ICSID arbitration and jurisdiction ratione materiae, jurisdiction ratione personae is one of the vital elements required by the ICSID Convention\(^2\) to submit legal disputes to ICSID arbitration. In lack of any of the three conditions, jurisdiction of an ICSID arbitral tribunal to settle a certain dispute will be denied. The latter can be done either by the Secretary-General of ICSID still before the registration of the request to arbitrate\(^3\) or, provided that the Secretary-General registered the request, by the respective arbitral tribunal which has the right to make a decision on its own jurisdiction\(^4\).

Provisions on ICSID jurisdiction are set in Articles 25 to 27, while jurisdiction ratione personae is governed by Article 25 (1) and (2). In the following, these two paragraphs will be analysed with special regard to practical issues as well.

2. Elements of jurisdiction ratione personae

The ICSID Convention sets forth the following provisions concerning jurisdiction ratione personae:

Article 25

(1) The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally.

(2) "National of another Contracting State" means:

\(^1\) International Centre for Settlement of Investment Disputes
\(^3\) Art. 36 (3) ICSID Convention
\(^4\) Art. 41 ICSID Convention
(a) any natural person who had the nationality of a Contracting State other than the State party to the
dispute on the date on which the parties consented to submit such dispute to conciliation or
arbitration as well as on the date on which the request was registered pursuant to paragraph (3) of
Article 28 or paragraph (3) of Article 36, but does not include any person who on either date also
had the nationality of the Contracting State party to the dispute; and

(b) any juridical person which had the nationality of a Contracting State other than the State party to
the dispute on the date on which the parties consented to submit such dispute to conciliation or
arbitration and any juridical person which had the nationality of the Contracting State party to the
dispute on that date and which, because of foreign control, the parties have agreed should be treated
as a national of another Contracting State for the purposes of this Convention.

Based on the latter provisions, the following elements of jurisdiction ratiocine personae can be
derived. Firstly, a Contracting State or any constituent subdivision or agency of a Contracting State
designated to the Centre by that State shall stand on one side.

On the other side, there must be an investor being the national of another Contracting State. The
investor party to the dispute can be either a natural or a juridical person.

The only requirement of the Convention with regard to natural persons is that on certain dates\(^5\) they
must bear the nationality of a Contracting State other than the State party to the dispute. The case is
not so simple as to juridical persons which, on the one hand, are eligible for ICSID jurisdiction if it
had the nationality of a Contracting State other than the State party to the dispute on the date on
which the parties consented to submit such dispute to conciliation or arbitration. On the other hand,
there is a special opportunity for juridical persons having the same nationality as the State party on
the date on which the parties consented to submit such dispute to conciliation or arbitration. If such
a juridical person is involved in the dispute and the parties have agreed that because of foreign
control that juridical person shall be treated as a national of another Contracting State for the
purposes of the Convention, the jurisdictional requirements are also met.

So much is provided for in the ICSID Convention. The exact meaning of those provisions, i.e. the
identity of the State party, constituent subdivisions and agencies, the identity of the investor party,
natural and juridical persons, will be dealt with separately hereinafter.

3. The identity of the State party

Identification of a State party is not difficult, the list of Contracting States is registered at the ICSID
Secretariat continuously\(^6\). It is important to mention at this point which states can become ICSID
Contracting States. Pursuant to Article 67 of the ICSID Convention, the Convention shall be open
for signature on behalf of States members of the Bank. It shall also be open for signature on behalf
of any other State which is a party to the Statute of the International Court of Justice and which the
Administrative Council, by a vote of two-thirds of its members, shall have invited to sign the
Convention.

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\(^5\) On the date on which the parties consented to submit such dispute to conciliation or arbitration as well as on the date on
which the request was registered pursuant to paragraph (3) of Article 28 or paragraph (3) of Article 36.

there are 154 signatories to the Convention 140 of which have deposited the instruments of ratification.
4. Constituent subdivisions and agencies of a Contracting State

It is a slightly more complex issue to determine what is a constituent subdivision or agency of a Contracting State and whether it is authorized to act as a party in ICSID arbitration proceedings. These concepts have a different meaning with regard to different Contracting States but exactly this is the reason why the drafters of the Convention did not give any clarification but left it for the Contracting States to designate those constituent subdivisions and agencies which can be involved in ICSID arbitration proceedings.

The term ‘constituent subdivision’ covers a broad range of entities, depending on whether a particular state is a unitary or a non-unitary state. In unitary states, municipalities and local government bodies fall under this category, whereas in non-unitary states semi-autonomous dependencies, provinces or federated states.

The range of ‘agencies’ covers entities acting on behalf of the government of the State or one of its constituent subdivisions. Government-owned companies or government-controlled corporations might fall under this category as well but the decisive factor, here too, is that the latter must act on behalf of the State, mere governmental ownership of shares is not enough.

Designation of constituent subdivisions and agencies to the Centre must be made formally, a mere designation or undertaking in the investment agreement, or a mere agreement between the State and the constituent subdivision or agency is not sufficient for the purposes of the Convention. It is also arguable that if the intention of the parties was to designate a constituent subdivision or agency but this had not been done officially by the respective State, then if designation was brought to the attention of ICSID by any of the parties would be sufficient. On the other hand, an agreement between the parties to the investment and in which the Contracting State itself designates the constituent subdivision or agency suffices as a proper designation.

As to the time of designation, the latest point of time for a designation to be made is the filing of the request to arbitrate. If the designation is not made at that time, the Secretary-General, pursuant to Article 36 (3) refuses to register the request.

It is an additional requirement set forth by the Convention, relating to one of the other two main conditions of jurisdiction, that when a party to the dispute on one side is a constituent subdivision or agency, the consent to be given must be of special nature as well. Pursuant to Article 25 (3) consent by a constituent subdivision or agency of a Contracting State shall require the approval of that State unless that State notifies the Centre that no such approval is required. The latter has been done by Australia, Peru, Portugal and the United Kingdom in their designations of constituent subdivisions or agencies. In respect of all other Contracting States, consent by a constituent subdivision or agency of a Contracting State shall require the approval of that State.

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7 Based on paras (1) and (3) of Article 25 ICSID Convention. See http://www.worldbank.org/icsid/pubs/icsid-8/icsid-8-c.htm
8 Practical examples are: Australia designated the States of New South Wales, Victoria, Queensland, South Australia, Tasmania, The Northern Territory and The Australian Capital Territory as constituent subdivisions; the United Kingdom designated Bermuda, British Virgin Islands, Cayman Islands, Falkland Islands, Dependencies, Gibraltar, Montserrat, Anguilla, St. Helena, St. Helena Dependencies, Turks & Caicos Islands, Bailiwick of Guernsey, Bailiwick of Jersey and the Isle of Man as its constituent subdivisions.
9 For example Ecuador designated Corporación Estatal Petrolera Ecuatoriana and Consejo Nacional de Electricidad; Nigeria designated Nigerian National Petroleum Corporation; and Sudan designated the General Petroleum Corporation.
Validity of such approval is an important prerequisite. A valid approval can be given in an agreement with the host state or in a separate designating instrument. In either case, however, approval must be express and unambiguous and must be given at least prior to the filing of the request. On the other hand, it is not necessary for an approval to be valid to communicate it to the constituent subdivision or agency and acceptance of the approval by the latter is not required either. It is also not necessary, pursuant to the wording of the Convention, that the approval be communicated to ICSID. This means that the approval, once given in the appropriate form, is valid and cannot be withdrawn. Yet, at the filing of the request to arbitrate the requesting party will have to give information on whether the consent to arbitrate was approved by the respective Contracting State, otherwise the Secretary-General will refuse to register the request.

In practice it is not only useful but also vital to make sure whether a certain constituent subdivision or agency is authorized to take part in ICSID arbitration proceedings and to include this in the arbitration agreement as well. For example if, at the time of contracting, the exact identity of constituent subdivisions or agencies to be involved cannot be identified because of the elongated nature of the investment or because the investment is to be carried out in several, not yet completely determinable stages, the arbitration clause should contain general phrasing which is eligible to mean and include any constituent subdivision or agency. If such preparatory steps are not taken in advance, the registration of the request may be denied by the Secretary-General or later the arbitral tribunal may find that since the ratione personae requirements are not met, the tribunal does not have jurisdiction to hear the case.

5. Identity of the investor party

As shown above, the investor party can be:

5.1. Natural persons

At first sight, determination of nationality is not complicated with regard to natural persons. Looking at the customary international law requirements of determining nationality, the International Court of Justice gave helpful guidelines in the Nottebohm case\(^\text{10}\). In that, basic attributes of nationality are a social fact of attachment, a genuine connection of existence, interests and sentiments and the existence of reciprocal rights and duties. However, usually the basis of determining nationality is the municipal law of the country in question, and only if this is not explicit can the Nottebohm decision be used. If a tribunal does so, then nationality can be substantiated by it even though nationality is not clear with regard to the state, the nationality of

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\(^\text{10}\) The Tribunal referred to the Nottebohm case in *Marvin Roy Feldman Karpa v. United Mexican States* (Case No. ARB(AF)/99/1) where it was ruled that jurisdiction does extend to the Claimant being a US citizen but having his permanent residence in Mexico since citizenship and not residence is the main criterion to decide upon nationality. We must also note that this particular case involved the NAFTA Agreement which provides for additional jurisdictional requirements.
which the natural person has upon the decision and even in cases where that state did not regard that natural person as its citizen.

In the case of the Convention, however, all that is required to ascertain the nationality of a natural person is a relationship with a Contracting State, irrespective of whether that state claims him to be its national for other purposes, and there is no requirement that he natural person prove that the Contracting State in fact makes this claim. On the other hand, in *Emilio Agustín Maffezini v. Kingdom of Spain*\(^\text{11}\) the Tribunal decided that Artcle 25 of the ICSID Convention shall be read together with the relevant provisions of the bilateral investment treaty (BIT) with regard to the nature of investment and in order to assess the capacity of the parties. Based on the latter argumentation, the Tribunal ruled that Claimant, “an Argentine investor in a Spanish company, who brings this action ostensibly to protect his investment in that company and for losses incurred by him due to injurious acts he attributes to Respondent. If proved, these facts would entitle Claimant to invoke the protection of the BIT in his personal capacity. (Convention, Art. 25; BIT, Arts. I(2) and II(2)). Accordingly, Claimant can be said to have made out a *prima facie* case that he has standing to file this case.”\(^\text{12}\)

There are limitations as to nationality requirements. For example there might be cases where the natural person involuntarily acquired the nationality of the host state, and therefore the requirement of the Convention that the natural person must have a nationality of a Contracting State other than the host state is not fulfilled; or, the natural person may involuntarily acquire the nationality of another Contracting State but he would not be regarded as having the nationality of that state. In such case, the principle is that “where the nationality of a Contracting State is assumed by a person when he does not have a reasonable connection with that State just before the consent to jurisdiction is given and in circumstances in which both he has lost the nationality of a non-Contracting State by that act and his closest connection has been for some time with the host state, it might be held that he does not have the nationality of a Contracting State for the purposes of the Centre’s jurisdiction”\(^\text{13}\). In cases where the change of nationality was from that of a Contracting State other than the host state to another or if the new nationality was from a condition of statelessness, if the closest connection has not been with the host state, the nationality of the natural person is usually not disregarded. However, if the nationality was acquired by fraud or mistake, that nationality shall be ineffective and disregarded.

As to stateless natural persons, the general view is that these persons do not have locus standi in ICSID arbitration proceedings unless the nationality of a Contracting is somehow attributed to them.

There are important issues regarding dual and multiple nationality, too. In the case where a natural person is a national of a Contracting State other than the State party and of the State party at the same time, the dispute is excluded from ICSID jurisdiction.\(^\text{14}\) The latter cannot be excepted either by an agreement with the host state or by the fact that the host state was aware that the natural person had its nationality. However, in cases where for special reasons it is held that such nationality shall be disregarded.

In multiple nationality cases one can assume that a natural person with a nationality of another Contracting State, irrespective of whether he also has the nationality of a third Contracting State or of a non-Contracting State, falls under the jurisdiction of ICSID since what matters here is that one of the natural person’s nationalities is that of another Contracting State.

\(^\text{11}\) *Emilio Agustín Maffezini v. Kingdom of Spain* (ICSID Case No. ARB/97/7)


\(^\text{13}\) Amerasinghe [1977]

\(^\text{14}\) Of course the case where the natural person is a national of a non-Contracting State and any other state, the fact that one of its nationalities is of a non-Contracting State automatically excludes jurisdiction.
As to the time when the nationality requirements are to be fulfilled, the Convention provides that it must be done both at the time of the consent to jurisdiction and at the time at which the request for arbitration is registered. It is important to note that there is no requirement of continuity between these two dates and there is also no requirement that the natural person must have the same nationality on these two dates. It may happen that at the time of the filing of the request the nationality requirement is fulfilled but ceases to do so shortly afterwards but still before the registration. In that case, the Secretary-General, not knowing about the latter, will register the request but it can be objected to later before the tribunal.

5.2. Juridical persons

However, most foreign investments are carried out not by natural but juridical persons, the nationality of which is usually determined by the siége social or the place of incorporation.

The term ‘juridical persons’ is not defined by the Convention because it is desirable to leave a broad range of definition since every country has a different perception on the issue. Otherwise, it is the task of the arbitral tribunal to decide whether, for the purposes of the Convention, a certain entity qualifies as a juridical person.

On the other hand, if the host state decided either that a certain entity is regarded as a juridical person or that it is not, that usually has some, yet not binding, effect on the tribunal deciding upon the question. Apart from cases of fraud and similar circumstances leading to mistake, the arbitral tribunal may decide to disregard such an election where it is clear that neither according to the law of the host state nor the law of the state whose nationality is claimed leads to the fact that the party has juridical personality.

5.2.1. Locally incorporated companies

Article 25 (2) b) of the Convention provides for a special aspect of jurisdiction where the latter extends to a juridical person which had the nationality of the Contracting State party to the dispute on the date on which the parties consented to submit such dispute to arbitration and which, because of foreign control, the parties have agreed should be treated as a national of another Contracting State for the purposes of the Convention.

This case is common in practice when the host state requires the investor to create a company within the host state and carry out the investment through this locally incorporated company. In this case, equity desires to give the investor the right to refer disputes to ICSID even if the locally incorporated company is obviously not a national of a Contracting State different from the host state.

In such cases, special attention shall be paid to appropriate phrasing with regard to the fact of foreign control, the nationality of those foreign controllers and the explicit agreement to treat the locally incorporated company as a national of the Contracting State of which the foreign controllers are nationals. It is not enough, for example, if the parties to the agreement solely lay down that “the nationality requirement is fulfilled”. A detailed description of the exact situation, all aspects of control and an explicit agreement is needed in order to avoid any problems or misinterpretations.

The following issues emerge in relation to ICSID jurisdiction over locally incorporated companies: the form of the agreement on nationality, the nature of foreign control along with its existence, nationality, form and extent.
5.2.1.1. Agreement on nationality

Firstly about the form of the agreement on nationality. Although the Convention does not require any specific form for it, in practice, it is usually done in the consent agreement and it must be explicit. This can be done by, for example, stating that the investor does not have the nationality of the host state or that the nationality requirements are fulfilled but such ambiguous phrasing is not enough. The best way to express the agreement on foreign nationality is to lay down that the investor is the national of a certain state. Model Clause 7 specifically provides for that situation so that the parties can make sure that their agreement on nationality will not be challenged later (“It is hereby agreed that, although the Investor is a national of the Host State, it is controlled by nationals of name(s) of other Contracting State(s) and shall be treated as a national of [that]/[those] State[s] for the purposes of the Convention.”). On the other hand, there is a growing tendency to accept implicit agreement, too.

Let us see some practical examples on the issue. In the very first ICSID arbitration proceedings, Holiday Inns v. Morocco arbitration was requested by the four H.I.S.A. Companies, locally incorporated corporations of the foreign investor Holiday Inns. The H.I.S.A. Companies were not parties to the original agreement containing the consent (they hadn’t even existed at that time) and not any rights were assigned to them either. The Moroccan government insisted that since there was no express consent to treat them as foreign nationals, jurisdiction did not exist. The Claimants argued that the H.I.S.A. companies had been set up in the interest and upon request of the Moroccan Government which, on the other hand, had always considered them as foreign controlled entities. The Tribunal did not deny that implicit agreement on nationality would theoretically be acceptable but it also expressed that it can only be effective under special circumstances which would exclude any other interpretation, and this was not the case here.

In Amco v. Indonesia the arbitration clause named the locally incorporated company, PT Amco as a potential party to ICSID arbitration and Amco Asia, the original party assigned its rights to PT Amco. This could seem an unambiguous case but Indonesia still objected to jurisdiction on the ground that it had not expressed its agreement to treat PT Amco as a foreign national. Amco argued that no formal requirement was necessary thereto and the Tribunal agreed. It found that only two main conditions were to be fulfilled, namely that the juridical person must legally be a national of the Contracting State which is the other party and the juridical person under foreign control must be treated as a foreign juridical person to the knowledge of the Contracting State. In the instant case the Tribunal found that the documents proved that PT Amco was an Indonesian company under foreign control. Therefore, the Tribunal also stated that in the case at hand, the agreement was not implied but because of using expressions like ‘foreign business’, ‘foreign capital’ in the documents, the agreement on nationality was clearly expressed.

In Klöckner v. Cameroon the foreign investor took part in the establishment of a joint venture company (SOCAME) in Cameroon. An establishment agreement between SOCAME and Cameroon contained an ICSID clause, at the time of which Klöckner owned 51 and Cameroon owned 49 percent of the SOCAME shares. The validity of the arbitration clause was questioned on the ground that SOCAME was a Cameroonian company. The Tribunal made a simple, logical ruling when stating that the mere existence of an ICSID arbitration clause indicated an implicit agreement on foreign nationality.

16 Holiday Inns S.A. and others v. Morocco (Case No. ARB/72/1)
17 Amco Asia Corporation and others v. Republic of Indonesia (Case No. ARB/81/1)
18 Klöckner Industrie-Anlagen GmbH and others v. United Republic of Cameroon and Société Camerounaise des Engrais (Case No. ARB/81/2)
In *LETCO v. Liberia* the locally incorporated company was fully owned by the French investor and the concession agreement between the parties contained an ICSID arbitration clause without any agreement on foreign nationality. The ruling of the Tribunal was similar to what was said in Klöckner *v.* Cameroon, i.e. the mere agreement to ICSID jurisdiction implies such an agreement.

As seen above, implied agreement on foreign nationality has become a practice but this is not without criticism. Firstly, because not every expression of consent equals the fact that there has been an agreement on nationality as well, only in those cases where the investor and the host state were in immediate contact. If the consent was given in a domestic source of law or in a treaty, the submission to ICSID jurisdiction by itself cannot serve as an implied agreement on foreign nationality.

### 5.2.1.2. The existence of foreign control

Foreign control is an objective requirement which must be examined independently of the foreign nationality. However, causal relationship is needed between the control and the agreement, yet it has also been argued that the agreement on nationality by itself assumes the existence of foreign control.

Determination of the foreign nationality was done in several ways in different cases. In *Amco v. Indonesia* the nationality of the direct controller was taken into account, in *Klöckner v. Cameroon* the majority rate of shares served as a basis. In *SOABI v. Senegal* the Tribunal made a very important conclusion, namely that where there was an agreement that the nationality requirements were fulfilled, the party that contested the effect of this agreement had the burden of proving that the requirement of control was not fulfilled. The Tribunal also analysed the question whether direct or indirect foreign shall be taken into account but this issue will be dealt with later. In *LETCO v. Liberia* the Tribunal examined the causal relationship between foreign control and the agreement on nationality and found that where foreign control exists, the agreement to treat the company as a foreign national is because of this foreign control. This means that all that is required for the purposes of Article 25 (2) b) is the objective fact of foreign control, the host state’s awareness of the latter and a valid consent to ICSID jurisdiction.

In *Vacuum Salt v. Ghana* the Tribunal noted that there is previous practice to infer an agreement on nationality from the mere existence of an ICSID arbitration clause, yet noted that in those cases the objective existence of foreign control was presumed. A significant consequence of the latter is that while agreement on foreign nationality may be inferred from the consent agreement but the same is not possible with regard to foreign control.

### 5.2.1.3. Nationality of foreign control

The Convention does not give a clear explanation whether foreign control shall be done by nationals of another Contracting State or any other, even non-Contracting, state. Only one element is sure – controlling entities must be nationals of a state other than the host state. WHATSOEVER, if we take a close look at the wording of the Convention, it seems clear that ‘foreign’ covers a broader range than ‘of another Contracting State’. Yet, for the purposes of the Convention only foreign control by nationals of other Contracting States is acceptable, since, even in the initial situation, the investor

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19 Liberian Eastern Timber Corporation v. Republic of Liberia (Case No. ARB/83/2)
20 Amco Asia Corporation and others v. Republic of Indonesia (Case No. ARB/81/1)
21 Klöckner Industrie-Anlagen GmbH and others v. United Republic of Cameroon and Société Camerounaise des Engrais (Case No. ARB/81/2)
22 Société Ouest Africaine des Bétons Industriels v. Senegal (Case No. ARB/82/1)
23 Liberian Eastern Timber Corporation v. Republic of Liberia (Case No. ARB/83/2)
24 Vacuum Salt Products Ltd. v. Republic of Ghana (Case No. ARB/92/1)
party must be a national of ‘another Contracting State’ and not of any other state other than the host state.

Looking a little bit further, the phrasing ‘because foreign control’ implies another important issue, namely that the foreign control must correspond to the agreed nationality.

If we examine some practical examples, it will be clear that determining the nationality of the foreign controller is not always as easy as it seems. In *Amco v. Indonesia* the true controller of the locally incorporated PT Amco company was not the party to the original investment agreement (Amco Asia) but the latter itself was under the control of Mr. Tan, a Dutch citizen residing in Hong Kong who controlled it through his fully privately owned Hong Kong company. Yet, the Tribunal found that only direct, first-grade control can be taken into account.

A contrary decision was made, with regard to the admissibility of direct or indirect control, in *SOABI v. Senegal*, at the time of the investment procedure, the investor, SOABI was controlled by company Flexa being a national of Panama. Panama was not a Contracting State and therefore Senegal objected to ICSID jurisdiction claiming that jurisdictional requirements would be fulfilled only if SOABI had been controlled by a company being a national of a Contracting State. The Tribunal accepted this argumentation but also found that Flexa itself was under Belgian control and since Belgium was a Contracting State, ruled that indirect control is also enough to fulfill the jurisdictional requirements of Article 25 (2) b).

Although the decision in SOABI v. Senegal is widely recognized among commentators, the best approach would be to look at the true controller at all times regardless of whether it controls directly or indirectly.

### 5.2.1.4. Form and extent of control

What activities or facts can serve as the basis of such foreign control? There are many examples like capital or share ownership, different voting rights attached to different shares, decision-making procedures and exercise of management or know how but practically the scene is usually much more complex.

In *Amco v. Indonesia* reference was made to sole or main shareholding with regard to the indirect controller, in *Klöckner v. Cameroon* the majority control of foreign interests was examined just like in *SOABI v. Senegal* but here, above the latter, the nationality of the members of the Board of Directors was also taken into account. In *LETCO v. Liberia* also majority shareholding was the basis along with the analysis of the decision-making structure and management. A more interesting and thorough decision was made in *Vacuum Salt v. Ghana* where the Claimant asserted that the company was controlled by a Greek national although he owned only 20 percent of the shares but he and his wife were directors of Vacuum Salt. The remaining 80 percent of shares was in the hands of Ghanaian nationals. The Tribunal contended, however, that the Greek national served merely as a...

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25 Amco Asia Corporation and others v. Republic of Indonesia (Case No. ARB/81/1)
26 ICSID Case No. ARB/82/1
28 Amco Asia Corporation and others v. Republic of Indonesia (Case No. ARB/81/1)
29 Klöckner Industrie-Anlagen GmbH and others v. United Republic of Cameroon and Société Camerounaise des Engrais (Case No. ARB/81/2)
30 Société Ouest Africaine des Bétons Industriels v. Senegal (Case No. ARB/82/1)
31 Liberian Eastern Timber Corporation v. Republic of Liberia (Case No. ARB/83/2)
32 Vacuum Salt Products Ltd. v. Republic of Ghana (Case No. ARB/92/1)
Andrea Vincze

technicality and there was no evidence that he acted or was influential in a truly managerial function. Therefore, the Tribunal found that there was no foreign control.

Another aspect of the agreement on foreign nationality is the relevant time at which the nationality requirement shall be fulfilled. Under the Convention this time is at which submission to the jurisdiction of the Centre is consented to. Therefore, if the control changes during the course of the investment, special regard shall be paid in order to fulfil the jurisdictional requirements.

There is one more question relating to the choice of foreign nationality. The issue of unreasonable choices of the parties, e.g. in order to bring into the scope of ICSID jurisdiction disputes which would not normally fall under it, is not explicitly governed by the Convention. Yet, although there is no explicit prohibition of such acts, it seems reasonable to refuse to accept as valid those agreements in which a totally unconnected nationality was chosen.

5.3. Other possible actors on the investor’s side

Besides, the question arises whether a government of another Contracting State may appear as the investor party, either alone or together with a national of its own. The answer is clear: the wording of the Convention does not provide for a government to act as an investing party in any case. Even if there may be situations where a government stands along with a natural or juridical person investor, ICSID jurisdiction does not extend to the former. Another ambiguous situation may be when the Contracting State gave an investment guarantee to its national or insured the investment under the investment insurance scheme. During the drafting of the Convention several opinions emerged and there were plans to include a provision on giving the opportunity to the Contracting State to appear in the proceedings in such cases when the host state gave its consent and special conditions were met. In the end, however, no such provision was included in the Convention. Therefore, the answer to the initial question is no.

The question whether governments can play a role on the investing side also gives rise to a further question: whether governmental agencies or corporations can be investors. According to the generally accepted opinion, wholly or partly government-owned companies which are practically indistinguishable from the completely privately owned enterprises with regard to legal characteristics and activities qualify as ‘nationals of another Contracting States’ on the investor side.

6. Successors of the original parties

During the course of the investment agreement the identity of any party may change. The question rises, therefore, how one should consider such successions with regard to jurisdiction ratione personae.

In order to avoid any future disputes on the issue, it is useful to make an express provision in the investment agreement or any other document that the arbitration clause extends to possible successors in interest. In absence of such express clause, the arbitral tribunal will have to decide whether the scope of jurisdiction extends to the successors.

7. Real parties in interest after compensation

A number of States have developed schemes for insuring their nationals, generally through governmental agencies, against losses that may be suffered in relation to foreign investments. There are also at present two intergovernmental agencies—the Multilateral Investment Guarantee Agency and the Inter-Arab Investment Guarantee Corporation—that administer similar investment insurance schemes. If such a governmental or intergovernmental agency indemnifies an investor, the agency
will normally become subrogated to the investor's rights. The agency may nevertheless be unable to
avail itself of such agreement providing for the resolution of disputes under the Convention as may
originally have been concluded between the investor and the host State. This is so because ICSID's
facilities are not available for proceedings between governmental entities or between governments
and intergovernmental organizations. It may therefore be necessary that in any dispute the
proceeding be conducted by the investor.

Theoretically, the investment can be insured anytime but as the nature of an insurance is to avoid
dangers to that investment, insurance must be made well ahead of the time at which the investment
is to be made. This means that the parties will be aware whether there will be such an insurance
already at the time of drafting the investment agreement, therefore it is useful to include a clause
that the right to submit disputes to ICSID shall not be affected by the fact that, if a governmental or
intergovernmental agency indemnifies an investor, the agency will normally become subrogated to
the investor's rights.

Useful guidelines can be found in Model Clause 8 providing that “/i/t is hereby agreed that the right
of the Investor to refer a dispute to the Centre pursuant to this agreement shall not be affected by the
fact that the Investor has received full or partial compensation from any third party with respect to
any loss or injury that is the subject of the dispute [; provided that the Host State may require
evidence that such third party agrees to the exercise of that right by the Investor]”.

Conclusion

Ratione personae jurisdiction raises interesting questions both in theory and in practice. The latter
two, however, may differ and as more and more cases are submitted to ICSID jurisdiction some
tendencies and also derogations from the latter can be observed. This paper did not attempt to make
a thorough analysis of all practical cases from ICSID’s available caseload but the most important
issues were highlighted.

The core of the question is, however, that the Convention gives the parties a great deal of freedom
in providing for the elements of ratione materiae jurisdiction and such flexibility is a very important
overall feature of the Convention. The parties are restricted only in places where the agreement of
the parties is manifestly outside the scope of the Convention. Even where there are unclear or
ambiguous issues in a certain case, the purpose of the Convention is to apply the principle in
favorem jurisdictionis meaning that the parties’ original intent to submit the dispute to ICSID
arbitration shall be respected during the course of interpretation.

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