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Introduction

It is inevitable in the life of a lawyer that the pursuit of keeping your clients safe and happy does not always coincide with working on the legal issues that are of greatest interest at any given time to the individual lawyer.

We cannot complain however, our clients cause us to work on many challenging issues and areas which, left to our own devices, we might never have considered.

This then forms the background to the decision to create and write this short anthology of legal miscellany. Our e-book.

The articles are written on topics of personal interest to our lawyers.

We hope that each lawyer's enthusiasm and interest will thus be communicated to you the reader and may prove valuable in the same way our clients are to us: raising issues of interest and long term value which you might otherwise not have needed to consider.

Happy reading

JOHN GRAYSTON

The Origins of the State of the Union

The term refers to an annual statement made by the President of the United States of America to Congress. The address is required by Article II, Section 3 of the United States Constitution which states: “He [the President] shall from time to time give to the Congress information of the State of the union, and recommend to their consideration such measures as he shall judge necessary and expedient”.

Since 1790, the phrase “from time to time” has meant annually. The first memorable State of the Union address –then known simply as the annual message to Congress – was given by James Monroe in 1823 when he announced what became known as the Monroe Doctrine. It was also arguably in the most famous State of the Union address on May 25, 1961, that President John F. Kennedy committed the United States to “landing a man on the moon and returning him safely to the earth” by the end of the decade.

It is in this context that we consider the decision of the President of the European Union to institute Europe's own State of the Union address. Strictly speaking not possible prior to entry into force of the Lisbon Treaty in 2009 which created the European Union. The EU version of the State of the Union address is also an annual speech given by the President (of the European Commission) to the European Parliament. The first State of the Union in the European Union was given on 7 September 2010 by Commission President José Manuel Barroso and considered mainly issues of economic policy and employment. In his latest discourse in September 2013 President Barroso made what may in due course become a well known and well remembered statement when he called on *“all those that care about Europe, whatever their political or ideological position, wherever they come from, to speak up for Europe”.*

Not quite flying me to the moon but a start nevertheless.

Brief List of Misused English Terms in EU Publications

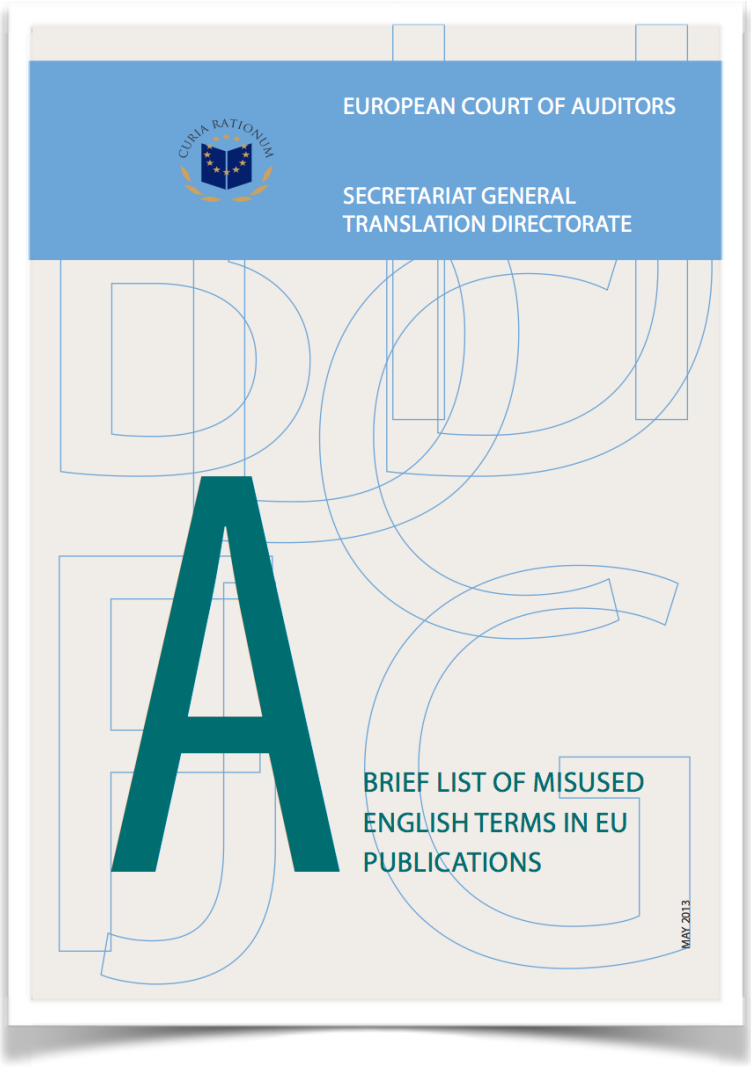
Linguistic errors and meanings of the EU .....

We have included in the book various extracts from what is my favourite publication of the EU this year. Full details of the document and its location are set out below:

Undoubtedly this is one of the best documents produced by the EU over the last year. It is also one of the most enjoyable to read.

We encourage everyone to have a look at the full work.
(Available as a free download here: http://ec.europa.eu/translation/english/guidelines/documents/misused_english_terminology_eu_publications_en.pdf *)*

We have taken the liberty of reproducing short extracts of the work at the beginning of each chapter in this eBook.



Detached

‘Detached’ means ‘separated’, ‘disconnected’ or standing apart from others *(as in detached house’)* or, in the case of a person, ‘marked by an absence of *(emotional)* involvement’. A ‘detached official’ would therefore be one who worked in an objective manner *(no doubt a laudable quality, but not what is usually meant)*.

Example

‘The table below shows staffing levels in ACP Delegations before and after devolution. External staff comprise Local Agents, Contract Agents, Detached National Experts and Young Experts.’

Laura Beretta

- International Trade Advisor

Laura Beretta is an Italian international trade advisor specialising in EU trade and customs law and Swiss preferential origin matters.

Her practice focuses on matters regarding free trade agreements, GSP regimes, tariff classification, rules of origin, customs valuation, origin marking, duty suspensions as well as exports controls and product conformity to EU standards.

Laura has been identified as one of the leading trade and customs experts by the International Who's Who Legal of Trade and Customs Lawyers.

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The New EU Generalised System of Preferences Rules of Origin:

The Opportunities for Complex Supply Chains and Challenges for SMEs

"Il proliferare dei regimi preferenziali rende complessa l'attività di ottimizzazione dell'imposizione daziaria connessa alle scelte di fornitura e di outsourcing. Tale attività però rimane irrinunciabile per ridurre l'impatto dei dazi pagati in ogni transazione cross-border compiuta dalle merci nelle diverse fasi di produzione e distribuzione. Questo articolo analizza i principali aspetti delle nuove norme dell'origine preferenziale applicabili alle importazioni dai Paesi beneficiari del Sistema Generalizzato di Preferenze dell'Unione Europea. A fronte di regole più flessibili e di maggiori opzioni di cumulo dell'origine, viene anche istituito un sistema di certificazione che creerà, al momento della sua entrata in vigore, nuove sfide e responsabilità per gli esportatori dei beneficiari e gli importatori UE."

Though reduced through multilateral negotiations and liberalised by the many existing preferential regimes, customs duties still impact significantly on trade in sensitive goods or with developing and emerging countries. Most notably, complex supply chains requiring semi-manufactured goods to move back and forth many times before the final output is obtained magnify the impact of customs duties, even when they are a small percentage.

This article examines the most beneficial changes brought by the recently reformed rules of origin applied by the EU to the importation of goods originating from developing countries in the context of its Generalised System of Preferences ("EU GSP").

1. The new EU GSP origin rules

Products imported from an EU GSP beneficiary country may be applied preferential duty treatment to the extent they are originating from that country in accordance with the unilateral EU GSP origin rules. The legal basis for this is Article 27 of Council Regulation No. 2913/1992, the Community Customs Code and Articles 66 to 97 of Commission Regulation No. 2454/1993, the provisions for the implementation of the Community Customs Code. Commission Regulation No. 1063/2010 has substantially reformed EU GSP origin rules, recently updated by Commission regulation No. 530/2013, to take into account some major changes of the new EU GSP which will be in force as of 1 January 2014.

The new rules generally allow more flexibility in purchasing and outsourcing strategies but also change, quite drastically, the system of origin certification which will be based on statements on origin given directly by the beneficiary country exporters.

Some major features of the following issues are outlined below:

- relaxation of list-rules and of conditions to apply regional cumulation;
- possibility of cross-regional cumulation and of extended cumulation;
- clarification of the meaning of simple operations in the context of insufficient transformations;
- inclusion of Turkey which has been added to Norway and Switzerland for the purpose of cumulation with GSP beneficiaries; and
- a new origin certification system.

2. More liberal product-specific list rules

Products are deemed to originate in a certain developing country if they are wholly obtained or substantially transformed in such country. Product-specific list-rules determine which transformations are necessary so that the product can acquire the origin of the beneficiary country where such transformations are performed. List-rules have been generally relaxed and differentiated, taking into account the diverse production capacity of developing and least-developed beneficiary countries.

This category of less advanced countries enjoys ad hoc and even more lenient list-rules. For example, ball or roller bearings acquire the EU GSP preferential origin of a beneficiary country if the customs value of non-originating materials utilised in the production process carried out in such beneficiary country does not exceed 50% of the ex-works price of the finished product. If the beneficiary country is a least-developed country, the threshold of allowed non-originating materials increases up to 70% of the ex-works price of the finished product. Quite differently the old list-rules provided two alternative options: according to the first option non-originating materials had to be classified under a different heading of the Harmonised System and their value could not exceed 40% of the ex-works price of the finished products; a second possibility was to utilise non-originating

materials upon condition that their customs value did not exceed the 25% of the ex-works price of the finished product.

3. New cumulation provisions

Regional cumulation is an important feature of GSP origin rules allowing the beneficiary country to confer EU GSP preferential origin to products obtained from materials originating from another beneficiary country of the same regional group.

Under the old rules there were three regional groups:

- Group I of ASEAN countries – Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar/Burma, Philippines, Singapore, Thailand, Vietnam;
- Group II – Bolivia, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Nicaragua, Panama, Perù, Venezuela; and
- Group III of SAARC countries: Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka.

A fourth group, composed by the MERCOSUR countries *(Argentina, Brazil, Uruguay and Paraguay)* is added with the new rules.

Under the previous cumulation rule, goods acquired the origin of the country of the regional group where the last working or processing was carried out provided:

i) that the value added there was greater than the highest customs value of the products originating in any other country of the regional group and
ii) that the working or processing carried out exceeded the insufficient operations.

Under the new regulation, materials originating in a beneficiary country of one group shall be considered as materials originating in another beneficiary country of the same group when incorporated in a product obtained there, provided that the processing performed in the latter beneficiary country exceeds the insufficient operations. The major change is that the value-added requirement has been dropped and it is sufficient that in the last beneficiary country operations going beyond the minimal ones are performed. Recourse to the value-added requirement will be necessary only if operations performed in the last beneficiary country are insufficient.

Another important change is the possibility of cross-regional cumulation between Group I *(ASEAN countries)* and Group III *(SAARC countries)*; cross-regional cumulation, however, does not automatically apply but is granted by EU Commission at the request of the authorities of a Group I or Group III beneficiary country.

Developing and least-developed countries can source productive inputs according to the flexibility allowed by cumulation and cross-cumulation if:

i) all beneficiary countries involved in the production comply with the EU GSP preferential origin rules and
ii) can provide the administrative cooperation among themselves and with the EU authorities necessary to the correct application of EU GSP preferential origin rules.

According to the new EU GSP regulation No. 978/2012, in force as of 1 January 2014, and the entry into force of bilateral free trade agreements with the Central American

countries as well as with Perù and Colombia, the scope of application of the new EU GSP will be reduced. Malaysia, Argentina, Brazil, Uruguay and Venezuela are among the countries that will lose the GSP preferences. Nevertheless, the other ASEAN countries will be still allowed to utilise inputs originating from Malaysia under the EU GSP origin rules. The same holds true for Paraguay, which is able to acquire products originating from Argentina, Brazil and Uruguay.

Furthermore, extended cumulation is envisaged by the new EU GSP origin rules. This new type of cumulation allows GSP beneficiary countries to utilise materials sourced from countries having a free trade agreement with the EU. The GSP beneficiary country will have to address the request to the Commission which will check if all the relevant conditions are met.

The list of insufficient transformations provides that certain operations, such as simple assembly, can never confer origin not even if through their performance list-rules are satisfied. Special skills, or machines, apparatus or tools are required to consider simple operations as origin-conferring. This clarification of what "simple" means is to be welcomed, especially for the assembly operations. Of course, whether a certain assembly is origin-conferring is to be determined on a case-by-case basis, but at least this clarification provides some useful guidance in borderline cases.

Turkey is added to Norway and Switzerland for the purpose of cumulation with beneficiary countries, meaning that goods obtained in GSP beneficiary countries and incorporating materials originating from Switzerland, Norway and Turkey will be considered as originating in these GSP beneficiary countries.

This type of cumulation is allowed provided that these three countries grant generalised tariff preferences to products originating in the beneficiary countries, apply a definition of GSP preferential origin corresponding to the EU one, and apply, by reciprocity, the same conditions to products originating in beneficiary countries incorporating materials originating in the EU. Turkey is still in the process of putting its GSP legislation in line with that of EU, Switzerland and Norway so these provisions are not in force. However, the possibility of supplying Turkish inputs to produce in beneficiary countries prior to exportation to the EU, or Switzerland or Norway is interesting due to the competitive costs of Turkish inputs in many sectors.

4. A new origin certification system

Origin certification will no longer rely upon origin certificates but will be based on a database of registered exporters. The idea behind this is to overcome a major shortcoming of the actual certification system, under which origin declared incorrectly does not necessarily result in the payment of duties by the importers, to the extent they acted in good faith and an error was made by the competent authorities. This principle is often at the basis of EU court cases on remission, repayment and non-recovery of customs debt.

The new system should be established as of 2017, but this deadline can be extended until 2020. Beneficiary countries' authorities will have the responsibility to designate registered exporters, to manage the database and respond to the EU requests and

verifications. On the other hand, new responsibilities are shifted onto the EU importers who, before declaring the goods, will have to take due precaution as regards:

- compliance of imported goods with the EU GSP origin rules;
- ensuring that the exporter is registered to make statements on origin regarding the products concerned and that such statements contains all the relevant information;
- when appropriate, requesting a written confirmation from the exporter that the exported goods have substantively acquired the preferential origin status under EU GSP origin rules.

5. Conclusions

The reformed EU GSP origin rules have substantially liberalised the conditions to be met by developing countries to enjoy the GSP unilateral preferences. The new cumulation rules allow more flexibility and options in the sourcing policies of beneficiary countries. The liberal architecture of the EU GSP rules of origin allows use of suppliers even in countries that have been removed from the GSP. Since the only bilateral preferential agreement enforced by the EU is the one with South Korea, the reformed EU GSP origin rules positively impact the supply chains based on Asian regional production networks. However, the new certification system that will be implemented most likely as of 2017 shifts new responsibilities onto EU importers who will have to take due precautions before claiming a reduced rate of import duty, something that will probably be troublesome for small and medium-sized enterprises.

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Intervention

In international relations, the normal meaning of ‘intervention’ is ‘interference by a state in another’s affairs’ and this can have strong negative connotations. Indeed, it is often found in combination with the word ‘military’[...] In EU parlance, on the other hand, it is just the term normally used to designate EU-funded operations in the member countries and elsewhere, and is part of a hierarchy of activities that also involves ‘measures’ and ‘actions’ in which, more of ten than not, ‘interventions’ are implemented via specific ‘measures’ and ‘actions’ are a subset of ‘measures’ *(sometimes known as ‘sub-measures’)*. However, confusingly ‘measures’ and ‘actions’, are sometimes just synonyms (as in the common pleonastic phrase ‘measures and actions’). A further problem is that, in normal English usage, both ‘intervention’ and ‘action’ are often uncountable, leading to unwanted grammatical problems. Curiously,‘intervention’ is also used to mean a ‘speech’ or ‘comment’, usually in a conference or meeting. This is also wrong.

Example

The following spoke: Holger Krahmer on the intervention by Rebecca Harm

Herbert Bayer

- Of Counsel

Herbert Bayer is a German qualified lawyer (Rechtsanwalt) and has a Diplom Finanzwirt (FH).

Herbert brings to our firm substantial experience of all aspects of customs law and procedure in Germany.

Herbert provides counseling to clients on customs compliance and general import/ exports strategies. He represents clients in Customs Audit procedures and in contentious proceedings before German Tax and other courts.

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Was für eine gute Idee! Etwas in Deutschland verkaufen.

How Hard Can It Be?

Drawing on years of experience in pointing out pitfalls to clients AFTER they have fallen in – Herbert Bayer lists some of the biggest customs and VAT heffalump traps to avoid.

Importing goods to the European Community is a very complex affair, with several issues that have to be considered. Even though customs law is directly applicable in every EU member country, the legal systems of the single Member States are quite different and so is the interpretation of the rules.

VAT is based on the Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax – "Umstazsteuersystemrichtlinie"[1]. Every member state has transferred this directive into its own VAT code. So the larger framework is actually the same but details can be very different. As an example, in the Netherlands import VAT can be liquidated with the VAT return while in Germany it has to be physically paid to customs. For input VAT, the German tax authority is in charge.

Also language does matter. In Germany the official language is German. § 87 Absatz 1 Abgabenordnung *(General German Tax Code)* states "Die Amtssprache ist Deutsch". Even though German customs and German tax authorities provide information in English, applications, communication and official statements have to be in German. If any document is needed they can ask for a translation. For VAT registration, the tax authorities provide questionnaires in English but the answers have to be in German.

The Community is working hard to harmonise the conditions for importing goods into the Community. One of their main targets is that process, demands and documentation for imports are similar no matter where the customs clearance is done. But language, history, development and self-conception of the authorities are not the same in the member states. They are not even the same in Germany where quite often cases can be treated very differently from Bundesland to Bundesland and also from local customs office to local customs office.

Keeping this in mind, I will use Germany as a basic example for importing goods to the Community in order to give you a first overview about the main points that should always be on your checklist when you plan to enter the German market. This is high level information and not complete but might assist you in to posing the right questions when structuring the import process and may help you avoid various pitfalls.

1. First Stop: Basics

From a legal perspective, customs and VAT regulations always have to be considered. Small changes in the supply chain can cause totally different results for customs and VAT treatment.

It is totally different if the goods are sold e.g. from China to Germany to a EU resident customer or if the goods are imported to Germany, stored first and then the customer is found. Especially in the automotive industry we can see that the major car producers ask for just in time delivery of goods that are in free circulation. Therefore the non resident supplier has to import the goods to the Community, clear them for free circulation and supply any goods just in time on single part ordering to the assembly line. There is no time for any delay and therefore the process has to be planned in detail.

Further taxes that are assessed on the import of goods are e.g.:

- Anti Dumping Duty
- Additional Duty
- Punishing Duty
- Environmental Fees
- and so on.
- Agricultural Duty
- Market Organisation Duty
- Excise taxes
- Local taxes and charges

Protection and prohibitions always should be on the checklist.

2. Who can do it?

If goods are sold to Germany and the German partner is responsible for the import customs, this might not be very interesting for the exporter because the resident buyer of the goods has to take care of all customs issues. But also in this case you should be aware of the import situation. It supports your situation during negotiations and is also the basis for controlling purposes.

In all other scenarios the first question might be: "Who can do the import?"

2.1. "Empfänger"

For Germany "Empfänger" *("Importer")* and "Zollanmelder" *("customs declarant")* have to be differentiated.

Actually Germans do not use the term "importer of record". It always leads to confusion, which can sometimes result in wrong solutions. Thus, at first it should be ensured that the understanding of any term used is the same.

The term "Empfänger" is the result of Community regulations which is especially used in the SAD[2]. In Germany the term "Empfänger" is equal to the term "Einführer" ("Importer") as used in "AWV – Außenwirtschatsverordnung" *(German External Trade Act)* and "AHStatDV - Außenhandelsstatistik-Durchführungsverordnung" *(German External Trade Statistic Implementation Act).*

"Einführer" is the person who brings or is responsible for bringing goods to Germany. If this person is a non-resident person, automatically the resident import contract party is considered to be the "Einführer".

In other words "Einführer" is normally the party of the contract that leads to the import who is resident in Germany or the Community. If there is no such person, the non-resident party is "Einführer". This is e.g. the case if goods are imported to a stock for a later sale without having a resident contract party. Provided goods are imported e.g. to a call-off-stock for a German car producer, it depends on the single circumstances whether the car producer can already be considered as importer.

The "Einführer" is the person who is responsible for ensuring that the import is in compliance with all import regulations. Therefore, the importer has to be in possession of any necessary import licence that may be requested.

The "Einführer" is also responsible for ensuring that the nature of the goods allows him to enter the German or Community market. If e.g. supplementary food is imported, the importer is responsible for ensuring the goods pass all control-, authorisation- or reporting-procedures in Germany as well as all protection or prohibition regulations.

In the past Germany requested a general import licence if the importer was not a resident person. This was, however, annulled a few years ago.

Special import licences e.g. for goods with limited import volumes-- quite common in the textile sector and for import of controlled goods such as drugs, arms and certain energy products authorisations --might be issued to resident persons only.

If there is no resident person available in such cases, imports can become impossible. In some cases bonded warehousing might be a solution. Sometimes establishing an EU resident branch might be a way out. But the branch has to have substance. A letter-box-company is definitely not enough.

2.2. “Anmelder”

“Anmelder” *(“customs declarant”)* is the person who applies for a customs procedure or a customs destination. If goods are cleared for the customs procedure “free circulation” , the customs declarant automatically becomes the import duty debtor.

The Community Customs Code claims that the customs declarant has to be able to present the goods to customs, provide customs with the corresponding documentation necessary for the applied customs procedure, and the customs declarant has to be a person that is resident in the Community.

A person that is not resident in the Community must not file any customs declaration. As a consequence, delivery terms that promise the supply of goods duty free should be avoided. But what to do if the customer demands a duty free delivery or if there is no resident available because there is actually no import contract?

Then representation might be a solution. The Customs Community Code allows everybody to use a representative. The representative, however, has to be again a resident person. The Customs Community Code offers two kinds of representation, direct and indirect representation.

Direct representation means that the representative acts in the name of and on behalf of the represented person. The customs declarant remains the represented person. This is the reason why direct representation does not work for non-resident persons.

The solution is indirect representation. Indirect representation means that the representative acts in his own name but on the account of the represented person.

The representative becomes the customs declarant. The customs declarant is automatically the import duty debtor. As a consequence of indirect representation, the represented person also becomes the import duty debtor in joint liability with the representative.

The reason for this complex situation is that the German authorities are only able to audit or enforce any open debts within the Community.

In Germany forwarding agents normally take care of import customs clearance. They are used to acting as direct representatives. They avoid indirect representation because of the risk that results from becoming the import duty debtor. An indirect representative is hard to find. If they offer the service of indirect representation, the fees are comparably high and security is necessary.

3. Calculating Duties

When goods are cleared for free circulation at least, customs duty and import VAT become due. Calculating duty is normally done in two steps.

At first customs duty and all other applicable duty with the exception of VAT is calculated.

The basis for calculating is normally the customs value. Market organisations sometimes use volumes or weight as a basis but this is more or less an exception. . Excise taxes have their own basis for assessment.

Custom duty is calculated: Customs value x customs duty rate = customs duty

If other duties are applicable they should be calculated now on the corresponding assessment base.

In a second step, import VAT is calculated:

Customs value
+ freight and insurance from point of entry to first destination
+ customs duty
+ further duties
= import VAT value x VAT rate
= import VAT

Duties that become due are the result of the sum of all assessed taxes.

In order to determine the import duty rates, the goods have to be classified. This is the subject of the next point followed by a few comments about customs valuation.

4. Classification

Before goods arrive at the Community customs territory, a pre-arrival message has to be sent to the customs office, which is in charge for the first point of arrival.

This has to be done in the corresponding customs IT-system of the EU member country concerned. For Germany this would be ATLAS. Normally the transporter is obliged to send this message.

Depending on the kind of shipment (e.g. vessel, airplane or truck) the deadlines are different. For sea-containers from the USA , the pre-arrival message has to be sent 24h before loading in the harbour of departure.

Customs use this information in order to make a risk analysis of the import. They decide on controls or use other methods of customs supervision. Therefore, any necessary information should be available before the export starts. This can be long before the import happens.

The basic requirement is the customs code. All goods have to be classified based on the TARIC *(Tarif Intégré des Communautés Européennes)*. The TARIC provides a ten digit code.

The basis for the TARIC is the six digits “Harmonised System” (HS) which is administrated by the World Customs Organisation (WCO). The aim of the WCO is to harmonise the nomenclature on a worldwide basis.

The Community adds two further digits to create the “Combined Nomenclature” (CN). Under the eight-digit-code of the CN duties, textile categories, protection and prohibitions and import license requirements are stated.

The ninth and tenth digit represent the TARIC that provides for measures such as anti dumping duty, duty suspensions or customs contingents.

The EU member countries use further digits in order to provide for national regulation such as VAT and protection and prohibitions. In Germany the customs code is called EZT “electronischer Zolltarif”. The EZT is part of ATLAS and uses 11 digits.

For certain goods, further four-digit codes can be added to the TARIC. The most common reasons for this are market organisations or excise duties.

Exporters should be aware that their domestic nomenclature and the TARIC only share the first six digits. The rest can be very different. And sometimes even the classification of chapters and position can be very dissimilar. On a world- wide level, harmonisation is far away. But normally the first six digits at least provide an orientation.

The TARIC is applicable in any member country. Therefore it should not matter to which country goods are imported. But also here the interpretation is very different. And also the national digits (11th and the following) have to be considered. The national code normally uses the official language of the country. In Germany the official language is German. The EZT is not available in any other language and sometimes it is very difficult to translate words and meaning.

Using the wrong customs code can have dramatic consequences. Import licenses can be overseen which makes the import illegal. Preferential proofs can be invalid. The wrong VAT rate can be applied which can make VAT a cost.

The EGZ shows the customs office in Germany the applicable duty rates but also which protections and prohibitions are applicable. Sometimes certain codes have to be used in the ATLAS customs declaration. For certain codes ATLAS performs automatic checks and the declaration will be refused if incorrect codes or no codes are used.

Finding the error is normally very complex for the declarant. If customs are not sure if the correct customs code is used they will check the shipment, taking samples if necessary. This can cause delays and stop the import.

With the customs code, duty rates and VAT rates can be determined. Therefore, the first information necessary for calculating and assessing import duties is now available.

The assessment basis for customs duties is normally the customs value.

5. Customs Valuation

Rules for customs valuation are stated in the Customs Community Code. These rules are based on the GATT Customs Value Code, which is not directly applicable in the Community but influences the interpretation.
The Customs Community Code offers six methods of customs valuation. The most important rule is the transaction value method.
If this rule is not applicable the other rules have to be applied in their order of appearance in the Customs Community Code. If rule one is applicable, rule two and the following are excluded. If rule one does not provide a result, rule two has to be checked before rule 3.

The rules are:

- Transaction value method
- Transaction value of identical goods
- Transaction value of similar goods
- Deductive Method
- Additive Method
- Reasonable means.

The customs declarant, however; can choose which shall be used first — the deductive or the additive method.

Customs valuation is one of the most complex issues of customs. Therefore only a few points shall be mentioned here.

Transaction value is the price actually paid or payable for the goods when sold for export to the customs territory of the Community, adjusted where necessary as stated in the Code.

Based on this legal definition, transaction value has to represent a sale. If goods are imported e.g. to a stock as an intra-company movement of goods or for leasing purposes or for commission, the transaction value method is not applicable. In most cases the following methods one to five do not lead to a result. Most times the necessary data is missing. Then “reasonable means” has to be used. The consequence of this method can be that the customs value is determined on the basis of the highest possible value.

If there is no sale it is necessary to prepare proper and conclusive documentation to face customs. A cost plus or a resale minus calculation can lead to proper results. Methods one to five have to be used analogously.

If nothing is done customs will challenge you and most times duties will be overpaid.

If exporter and importer are related, the transaction value method is only applicable if the price has been influenced in an acceptable way. German customs started to challenge in particular situations when transfer-pricing agreements contain clauses for compensatory payments.

In general transfer-pricing studies can support the argumentation for a customs value. But in general such a study cannot be transferred one to one for customs purposes. The intentions of transfer-pricing and customs valuation point in different directions. For

customs purposes, the customs value should be as low as possible. From a transfer pricing perspective, as little benefit as possible should be created because only the remaining profit is subject to company taxes. Transfer pricing reflects the profit situation in total while customs valuation is based on single goods that are imported. Therefore the effects of a transfer price agreement on customs valuation and vice versa should always be considered and checked.

The subject of the transfer price is a sales price agreed for an export to the customs territory. In a chain of supplies this can be any sale that fulfils this condition. In the Community "first sale" scenarios are still accepted. First sale, however, is a customs-planning tool that seems to be very simple to use. But since obviously less duty is paid customs will challenge it. The demands of customs with respect to documentation and proofs are very strict and detailed. If any mistake is made they will destroy the planning.

The customs community code shows a limited range of scenarios where the price actually paid or payable has to be adjusted.

Costs for packing, transport and insurance to the customs territory have to be included in the transaction value.

Royalties and license fees normally have to be added to the customs value provided they are due for the imported goods. Royalties for immaterial properties do not have to be added. However, if the immaterial property is reflected in the imported good, the fees are subject to the customs value. Labels and trademarks normally always have to be added. Royalty agreements always have to be checked very carefully. If any service is licensed you must consider that there has to be proof that the service is actually carried out. Otherwise the costs will be added to the customs value as royalty; If this is not clearly the case German customs treat it as side payment.

If the transaction value is not applicable or if any adjustment cannot be clearly determined, the transaction value method will not be accepted. Normally customs valuation will then end in "reasonable means". And "reasonable means" results normally in arguments with customs and overpayments and are likely to end in court.

After classification the duty rates can be determined on the basis of the customs value and duties can be calculated. But paying duties is not always the best solution.

Therefore a short overview of the possible customs procedures follows.

6. Customs Procedures Overview

Once goods are cleared for free circulation, normally there is no refund of customs duties possible if the goods are re-exported. If e.g. goods are imported to Germany for storage and a part of the goods is exported to Switzerland, clearing goods for free circulation in Germany and Switzerland might be a bad idea because customs duty becomes due in both countries.

Customs Clearance for Free Circulation

Customs clearance for free circulation is by far the easiest customs procedure. All duties are paid and then customs supervision ends.

A special alternative is clearing goods as returned goods. Goods which have been exported from free circulation without any duty refund can be re-imported under the returned goods regime with duty exemption. From a VAT perspective it is necessary that import VAT can be deducted, otherwise it will be assessed. For using “returned goods” proper documentation is necessary that shows the export of free goods without any refund.

Zolllager - Bonded Warehousing

Bonded warehousing suspends duty payment. The goods are stored. The bonded warehouse procedure ends when the goods are placed under a new customs procedure. This can be e.g. “clearance for free circulation”. Then duties become due. But it can also be “re-export” to a non EU member country like Switzerland or Norway in combination with a “transport procedure”.For bonded warehousing a formal authorisation has to be issued by customs. Different types of warehouses are available. Only persons resident in the customs territory can apply successfully for an authorisation.

Aktive Veredelung - Inward processing relief (IPR)

IPR is used if materials are imported into the EU, processed there and after processing the finished goods are exported. Then normally no customs duty is assessed when the materials are imported in the suspension alternative.

However, there is also a refund alternative. Then duty is assessed when the materials are imported, but a refund is granted when the finished goods are re-exported.

A formal authorisation is necessary for this procedure. Only persons resident in the customs territory can apply successfully for an authorisation. VAT scenarios are very difficult in this area and should be carefully checked.

Passive Veredelung - Outward processing relief (OPR)

OPR is the opposite of IPR. Materials are exported. The goods are processed in a third country. The finished goods are re-imported to the EU. Under OPR it is possible to reduce the duty payment by determining the theoretical duty of the materials which were exported at the moment when the finished goods are re-imported. There are different calculation methods.

A formal authorisation is necessary for this procedure. Only persons resident in the customs territory can apply for an authorisation.

Produktion unter zollamtlicher Überwachung -Production under Customs Control

Here materials are imported, processed and then the finished goods are imported for free circulation. Value is determined on basis of the finished goods. This procedure is used when the duty rate for finished goods is “free” but there is still duty on the materials. *(e.g. a mobile-phone with duty rate is free and camera-model is subject to duties).*

Vorübergehende Verwendung - Temporary use

For certain goods it is possible to import and use them in the customs territory. However the goods must not be processed and cannot be sold. This is the typical procedure for tourists or tools.

In some cases a formal authorisation is necessary for this procedure. Also non resident persons can use this procedure.

Versandverfahren NCTS – Transport

If non community goods are transported from one place in the EU to another, customs supervision has to be ensured. Therefore goods have to be placed under a transport procedure. The community knows the different procedures. In the customs territory normally the T1 procedure has to be used. It is done with an IT-Solution that is called NCTS *(New Computer Based Transit System).*

For simplification a formal authorisation is necessary for this procedure. In single cases the customs office in charge grants it.

Other

Goods in free circulation that are to be exported have to be placed under the export procedure. For goods that are not in free circulation the re-export procedure has to be used. This procedure is nearly identical to the export procedure. Both ensure export control.

Other customs designations are destruction under customs control and free zone storage.

7. Import VAT and VAT

In general import VAT is deductible as input VAT. Private persons or small entrepreneurs are normally not entitled to deduct import VAT. And there are a lot of exemptions for full entrepreneurs, which prohibit the input VAT deduction.

Normally only the owner of the goods at the time of importation is entitled to deduct import VAT as input VAT.

The customs declarant, the importer and the person who has the right to deduct the input VAT can be different.

The debtor who is entitled to input VAT deduction can deduct import VAT using the preliminary VAT return. If no registration is possible the “Vergütungsverfahren” is available if all conditions are met. For the later the deadlines and documentation are always critical.

VAT becomes due if any of the VAT-scenarios of the “Umsatzsteuergesetz - UStG” is fulfilled:

- Supply of goods
- Supply of services
- Intra Community acquisition
- Import; form a VAT perspective “import” is customs clearance for free circulation.

When we look at a regular import e.g. goods are sold from China to Germany and cleared for free circulation, the scenario “supply of goods” and the scenario “import” is applicable because the goods are sold and cleared for free circulation.

VAT is a tax where change of any detail matters and can lead to a total different VAT scenario. The customs clearance for free circulation can influence the VAT treatment. Therefore the process has to be structured very carefully in order to avoid VAT becoming a cost.

This shall be explained by the following example:

A company located in the USA *(US-Co)* is an internet-provider selling goods for computers in his internet-shop. US-Co is registered for VAT in Germany because many of the customers are German IT freaks.

US-Co ships the goods via a Parcel Service to Germany. US-Co's customers would normally not order if they have to deal with customs. Thus US-Co delivers duty free *(DAP customer).*

The supply chain was structured in a way that the Parcel Service had to clear the goods as the forwarding agent for free *(or do you mean free? Yes!)* circulation in indirect representation of US-Co.

US-Co received an invoice with freight charges and duty *(including import VAT)* paid to German customs from the Parcel Service.

When goods are cleared for free circulation import duties become due. From a VAT perspective the scenario "import" is applicable. So import VAT is assessed.

In the example described the Parcel Service should become the import duty debtor in joint liability with US-Co.

From a VAT perspective the scenario "supply of goods" is applicable as well. Thus the place of supply has to be determined. Normally the place of supply is where the shipment starts. This is in the USA where US-Co is located.

But if the supplier becomes the debtor of the import VAT, the place of supply is deemed to be in the EU member country where the goods are cleared for free circulation. The VAT code creates more or less the fiction that title of the goods is transferred at the place of supply. This is Germany, after the import. US-Co is still the owner of the goods at the time of importation. This is a result of the rule that shifted the place of supply from the USA to Germany. As owner at the time of importation US-Co is entitled to deduct import VAT.

As a consequence VAT has to be shown on the invoice from US-Co to its customer and US-Co has to register for VAT in Germany.

But in this case we had to deal with the parcel provider who acted as the direct representative in the name of and on behalf of the customer of US-Co. He simply feared the risk of indirect representation and he had all necessary information because the importer was the customer. Thus he cleared the goods on his behalf.

In direct representation, the import duty debtor is the represented person. This was the customer of US-Co.

The place of supply is where the shipment starts. This was in the USA. Since US-Co did not become the import VAT debtor, the rule used above is not applicable. The place of supply remains in the USA. From a German VAT perspective the supply is not taxable. The USA does not have a VAT system but they would treat this normally as a sales tax free export.

Since the place of supply is in the USA, title of the goods changes in the USA and owner of the goods at the time of importation is already the customer. Thus US-Co is not entitled to deduct the import VAT. If the customer is not entitled to deduct input VAT, import VAT will remain as cost.

US-Co has already issued the invoice showing VAT. It was in the parcel. VAT that is shown on an invoice has to be paid to the VAT authorities even though it is wrongly shown on the invoice. The customer, however, is not entitled to deduct this VAT as input VAT. The customer can ask for an invoice correction and if he paid VAT to US-Co he can ask for a refund.

At the end US-Co is at risk to pay:

- Import VAT to the forwarding agent *(the mistake is normally only realised later during an audit)*
- and VAT to the authorities, because it is wrongly invoiced.
- Due to the wrong place of supply the customer could correct his payment to US-Co and ask for compensation.
- There is no refund for the import VAT for US-Co and customers were normally not entitled to do so.

It is one of the easiest challenges for German VAT auditors to determine such mistakes. Correcting this situation is very time consuming and cost intensive. Normally not everything can be corrected. The rules for changes are very strict. Some tax offices do not allow global invoice correction. The number of customers made the situation very difficult. In some parts tax and customs authorities demanded that every case had to be treated separately. US-Co had to prove that the customer did not deduct the invoiced VAT as a condition to correct any invoices. As an result of this mistake, tax auditors visited bigger customers, knowing where to dig.

If US-Co had checked the process it would have been not to difficult to avoid the situation. In the planned process the customer would have been shown as the importer but not as the customs declarant on the duty assessment note. However , language, local rules and different customs IT solutions make it very hard to create, implement and supervise any customs related process. Working together with a local, native- speaking consultant can keep you out of pits.

Therefore, please structure your VAT processes carefully and check if it works.

We are always happy to help.

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Footnotes:

[1] *http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CONSLEG:2006L0112:20110101:EN:PDF*

[2] *SAD – Single Administrative Document / Einheitspapier.*

Foresee

The safest policy with this word is to avoid it. If you do wish to use it, bear in mind that it is one of the most frequently misused *(and, by many accounts, annoying)* words in this list and should be used with considerable caution. Its basic meaning in English is 'to see something in advance' and therefore to 'predict ' or 'expect'.

Example

'In total, Member States adopted 13 Fleet Adjustment Schemes (FAS), which foresee the scrapping of 367 vessels accounting for 32 448 GT and 50 934 kW.'

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Non-Tariff Barriers in WTO Law:

How Transparency Obligations Protect Traders

Dall'entrata in vigore dell'OMC, l'obiettivo del commercio internazionale si è spostato dalla lotta alle barriere tariffarie verso l'armonizzazione delle normative nazionali. Si è passati cioè da un regime di divieto (GATT 1947), ad un sistema volto a decidere ciò che gli stati membri devono e possono attuare a livello nazionale per essere compatibile con il WTO. In questo contesto, gli obblighi in tema di trasparenza si sono ampliati in nuove aree tanto da influenzare sempre di più la sovranità degli stati membri. Esempi sono gli obblighi di trasparenza nel settore dei servizi (GATS), della proprietà intellettuale (TRIPS) e delle misure sanitarie e fitosanitarie (SPS).

Introduction

Since its establishment in 1947, the GATT has provided dedicated commitments to transparency in trade administration *(Article X of GATT 1947)*. However, such commitments did not go beyond traditional trade barriers at the border, nor did they reach the domain of domestic regulatory systems embedded in the institutional infrastructure of each national economy.

Article X contains the most effective provision in the WTO system as to the so-called regulatory transparency. Article X is the first and most important provision to introduce regulatory transparency commitments to contracting parties in favour of international traders and governments. In a nutshell, Article X requests members to publish domestic law affecting international trade, forbids them from enforcing such laws until relevant publication, requires that such laws are administered in a uniform, impartial and non-

discriminatory manner, and lastly requires the establishment of tribunals or procedures for review of administrative actions.

Article X of GATT 1994

The text of Article X of the GATT 1947 has not been changed ever since its adoption; however, the appreciation and understanding of transparency principles among the stakeholders have varied dramatically in the last two decades.

With the entry into force of the WTO particularly, there are new provisions on transparency under the multilateral agreements of Annex 1A. This major change is primarily due to the shift from a model of negative regulation of GATT 1947, i.e. what the government is prohibited to do, to a positive approach highlighting what the government should do under the WTO.

One convincing explanation of such dramatic change is that the increase of interest around transparency is a direct consequence of the new policy target introduced by the WTO. The WTO has changed and expanded transparency beyond the GATT 1947 border to new areas that directly influence domestic regulatory regimes, such as in the area of services (GATS), intellectual properties (TRIPS) and sanitary and phytosanitary measures (SPS).

The growing complexity of international trade scenarios, the increased number of WTO Members and the diversity of domestic trade systems have also played a significant role in the widespread call for transparency.

In other words, transparency is the pivotal element to guarantee the compliance of WTO Members to their commitments.

In particular, it is vital to ensure:

(i) WTO Members can deter hidden commercial protectionist measures or political pressures on domestic regulators,
(ii) international traders are more easily aware of the several domestic legislations and
(iii) constraint upon the abuse of discretionary powers.

Article X commitments can be grouped into three-macro areas:

- Laws, regulations, judicial decisions and administrative rulings of general application, pertaining to the classification or the valuation of products for customs purposes, or to rates of duty, taxes or other charges shall be *published promptly* in such a manner as to enable governments and traders to become acquainted with them;

- No measure of general application taken by any contracting party effecting an advance in a rate of duty or other charge on imports, or imposing a new or more burdensome requirement, restriction or prohibition on imports, or on the transfer of payments therefor shall be enforced before such measure has been *officially published*;

Each contracting party shall administer in a *uniform, impartial* and *reasonable manner* all its laws, regulations, decisions and rulings of the kind described in paragraph 1 above.

Transparency under WTO judicature

It is beyond the scope of this publication to analyse in detail each of the specific commitments listed above. One should be aware, however, that the WTO jurisprudence had the possibility to investigate and specify the scope of the transparency commitments under Article X of GATT 1994.

In the *EC – ITA* case[1], for example, the Panel shed light on the criteria to judge if a measure falls under Article X:1. Whether a given measure constitutes a "law, regulation, judicial decision or an administrative ruling[2]" of general application within the meaning of Article X:1, this must be established on the basis of two precise elements: primarily,

(i) the *content and substance* of the measure at stake, and not merely its form or nomenclature and
(ii) if the measure has a *general application* nature.

Yet, in China – Auto Parts, the Appellate Body (AB) ruled that: "Laws, regulations, judicial decisions and administrative rulings" have to be interpreted to encompass more than those instruments formally characterised as such by the WTO Members.

Such wide interpretation aims to prevent departure from members in respecting its commitments; otherwise, WTO Members themselves would be free to determine in splendid discretion which provisions they wish to be scrutinised under the WTO obligations of Article X:1 of the GATT 1994. In EC – Selected Customs Matters, the Panel stated that: *"[T]he title as well as the content of the various provisions of Article X of the GATT 1994 indicate that Article, at least in part, is aimed at ensuring that due process is accorded to traders when they import or export […]"* [3]. *In United States – Restrictions on Imports of Cotton and Man-made Fibre Underwear,* it has been stated that Article X may be seen to embody a principle of fundamental importance – that of promoting full disclosure of governmental acts affecting Members and private persons and enterprises, whether of domestic or foreign nationality.

The essential implication is that Members and other persons affected, or likely to be affected, by governmental measures imposing restraints, requirements and other burdens, should have a reasonable opportunity to acquire authentic information about such measures and accordingly to protect and adjust their activities or alternatively to seek modification of such measures.[4] Lastly, in *EC Bananas III* and *EC Selected customs matters* the Appellate Body reasoned that the text of Article X clearly indicates that the requirements of uniformity, impartiality and reasonableness do apply to the administration of those laws, regulations, decisions and rulings.[5] The context of Article X:3(a) within Article X, which is entitled 'Publication and Administration of Trade Regulations', and a reading of the other paragraphs of this Article, make it clear that Article X GATT applies to administration of laws, regulations, decisions and rulings and not to the rules themselves. Thus, to the extent that the laws, regulations, decisions and rulings are discriminatory, they can be examined for their consistency with the other relevant substantive GATT provision. In *EC – Poultry*, for example, the Appellate Body made a reference to the above and concluded that the WTO-consistency of the substantive content of the [European

Communities'] rules challenged by Brazil in the present case must be determined by reference to provisions of the covered agreements other than Article X of the GATT 1994.[6]

Conclusion

Transparency commitments under the WTO are quite extensive and burdensome for the WTO member states. Under the current international trade regime, transparency is more and more used as an effective way to scrutinise the consistency of domestic policy of member states toward WTO rules. The considerable increase of its relevance witnessed in the last two decades has brought transparency under the spotlight today. Traders and governments should increase even more their use of transparency commitments since these are quite a valuable means to access foreign markets and prevent non tariff discrimination.

Footnotes:

[1] Panel Report, EC – ITA, para 7.1023-24.

[2] Panel Report, EC – ITA, para 7.1025 Substantively, a "law" is "a rule of conduct imposed by secular authority"; a rule which "a particular State [...] may enforce by imposing penalties". A "regulation" is "a rule prescribed for controlling some matter, or for the regulating of conduct; an authoritative direction". A "ruling" is "the action of governing or exercising authority, the exercise of government, authority, control, influence" or "an authoritative pronouncement". The adjective "administrative" indicates that it is a ruling from an administrative body. Finally, a "judicial decision" is an action or pronouncement by a judicial body or authority.

[3] Panel Report, EC- ITA, para 7.1015.

[4] AB Report, United States – Restrictions on Imports of Cotton and Man-made Fibre Underwear, section VI, pp. 21-22 (emphasis added by Korea).

[5] AB Report, EC – Bananas III, para. 200. See also AB Report, EC – Selected Customs Matters, para. 197.

[6] AB Report, EC – Poultry, para. 115.

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So-called

This is a risky term to use; although some dictionaries allow the meaning ‘commonly known as’, others, …. emphasise that its use casts doubt on the veracity of the term it introduces.

Furthermore, to cite the American Heritage Dictionary, ‘quotation marks are not used to set off descriptions that follow expressions such as so-called and self-styled, which themselves relieve the writer of responsibility for the attribution’. This use of ‘so-called’ followed by quotation marks is very common in EU texts *(second example)* and should be avoided.

Example

With dimensions of approximately 8,5 × 30 × 23 cm, designed for monitoring the respiratory and anaesthetic gases of a patient under medical treatment *(so-called ‘Gas Analyser Module’)*

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Towards EU-Wide Corporate Social Responsibility

Bevidsthed om Corporate Social Responsibility (CSR) er afgørende for virksomheder, der opererer på verdensmarkedet, hvor øget gennemsigtighed og kommunikation sætter fokus på et behov for fuldtud at overholde CSR normer. Selv med færre retlige forpligtelser og flere ikke bindende normer, så kan en undladelse af fuldtud at overholde disse normer føre til problemer og alvorlige skader på omdømmet. Udvikling af en overholdelsesstrategi for EU som helhed kunne være en løsning, men eftersom der kun findes en begrænset EU-regulering i bindende form, så står virksomhederne står over for en sammenblanding af nationale retlige foranstaltninger og ikke bindende normer.

Corporate Social Responsibility *(CSR)* is a concept that has developed over the last twenty years, with rapid and accelerating growth in public awareness and application during the last ten years.[1] Currently, it is a major concern for many companies and has become increasingly visible as front-page news in professional newsletters.[2]

However, it remains a field that is to a large extent unregulated, or regulated only by soft law. The purpose of this paper is to examine the latest developments in European Union *(EU)* policy on CSR and to present the experience of Denmark in supporting soft law targets with hard law measures.

The Development of Policy Goals in the European Union

The EU rests upon a principle of delegated competences.[3] The adoption of the Lisbon Treaty on 1 December, 2009, clarified this principle. This treaty modified the existing EU treaties and clarified the distribution of competences between the EU and its Member States, including areas with shared competence. These provisions do not address CSR, directly or indirectly. Accordingly, a competence falling outside the scope of EU competence remains with the each Member State.[4]

However, the interpretation of whether an area is within EU competence has some flexibility, even with a reserve provision setting the legislative procedure for areas that are not covered by more specific provisions.[5] The European Court of Justice *(ECJ)* has rarely overruled the assessment of the EU legislator about whether an area fell within EU legislative competence.[6] This flexibility is even wider in relation to non-legislative measures. The Lisbon Treaty codified competences to support Member State actions in broad fields of policy, including that of industry.[7] Thus, it seems clear that the EU has the competence to adopt non-legislative or soft law supporting measures concerning CSR. Further, arguably, hard law regulation of CSR is possible under the powers delegated to the EU regarding regulation of the Internal Markets.[8] Following the logic of one of the founding cases on gender discrimination,[9] one could argue that if CSR is not regulated in a similar manner in all Member States, the competition between companies will be upset when these companies come from Member States with differing levels of CSR regulation.

While this argument has an immediately convincing appeal, it also has an inherent danger. This would negate the principle of delegated competences. Accordingly, it has not become a main argument for the ECJ, except in the more limited form, where any national legislation that may have an impact on the internal market will be subject to EU limitations.[10] Thus, this argument is used to expand judicial, as opposed to legislative, competence.

In relation to CSR, the European Council seems to have followed the same conservative approach as the ECJ. This is illustrated by the conclusions of the Lisbon Meeting in 2001. The European Council has no legislative powers but has the task of setting the political and legislative strategy of the EU, which is subsequently implemented in coordination between the Council of Ministers, European Parliament, and European Commission.[11] The conclusions include the following statement in relation to CSR: "The European Council *makes a special appeal to companies' corporate sense of social responsibility* regarding best practices on *lifelong learning, work organisation, equal opportunities, social inclusion and sustainable development."*[12]

Evidently, the EU treats CSR as an industry-driven initiative for self-regulation. The EU wishes to support and urge industry to pursue CSR, but it does not intend to submit the industry to EU legislation. This supporting approach is further pursued in the 2001 Green Paper on CSR from the European Commission.[13] Green papers are normally used for presenting new legislative initiatives, so as to form the basis for a public hearing prior to the formal presentation of the legislative draft. However, it is clear that the intention of the European Commission is not to develop CSR legislation, but instead, to provide a framework to promote an industry consensus on the application of CSR. The Green Paper mentions the following goals of the Commission: *"Developing an overall European framework,* in *partnership with the main corporate social responsibility actors,* aiming at *promoting transparency, coherence and best practice* in corporate social responsibility

practices[]"[14] and "*[p]romoting consensus* on, and supporting, best practice approaches to *evaluation and verification* of corporate social responsibility practices[.]"[15]

These targets are further developed in the 2006 Communication on CSR from the European Commission.[16] The European Commission often uses communications to inform the public about its interpretation of the state of law. But, in this case, the communication is clearly aimed at the EU legislator to set the strategy of the European Commission. The main position taken by the Commission is that CSR is *"not a substitute for public policy,* but [] can *contribute* to a number of public policy objectives."[17]

However, the European Commission has also intended to address the industry, whose active participation in achieving the targets is clearly intended. The targets include:

- More *integrated labour markets* and higher levels of social inclusion, as enterprises actively seek to recruit more people from disadvantaged groups;
- Investment in *skills development, life-long learning and employability,* which are needed to remain competitive in the global knowledge economy and to cope with the ageing of the working population in Europe;
- Improvements in *public health,* as a result of voluntary initiatives by enterprises in areas such as the marketing and labelling of food and non-toxic chemicals;
- Better *innovation performance,* especially with regard to innovations that address societal problems, as a result of more intensive interaction with external stakeholders and the creation of working environments more conducive to innovation;
- A more rational use of n*atural resources* and reduced levels of pollution, notably thanks to investments in eco-innovation and to the voluntary adoption of environmental management systems and labelling;
- A more *positive image of business* and entrepreneurs in society, potentially helping to cultivate more favourable attitudes towards entrepreneurship;
- Greater respect for *human rights,* environmental protection and core labour standards, especially in developing countries; and
- *Poverty reduction* and progress towards the Millennium Development Goals.[18]

The ultimate goal is active participation of industry. This becomes clear when looking at the description of instruments that the European Commission intends to employ to reach the aforementioned targets. These instruments are described as actions; they are supporting measures, not legislative regulations. They include:

- Awareness-raising and best practice exchange with *an emphasis on Small and Medium-sized Enterprises (SMEs)*[19] and on Member States where CSR is a less well-known concept;
- Support to *multi-stakeholder initiatives,* including social partners and Non-Governmental Organisations *(NGOs);*
- Consumer information and transparency including clear *information on the social and environmental performance of goods and services* and information on the supply chain; and
- Research and education;[20]

With the Maastricht Treaty in 1992, the EU introduced the principle of subsidiarity, which requires that in areas outside of exclusive EU competence, the EU shall act only where it is not more relevant for Member States to act.[21] Although this principle has remained more of a political guide than a hard law provision subject to jurisdiction, it seems clear

that the European Commission had this in mind when drafting the proposed actions. The communication clearly demonstrates the cross-border implications and perspectives of CSR.

These implications include the following:

- International dimension of CSR – United Nations *(UN)* Millennium Development Goals, International Labour Organisation Tripartite Declaration of Principles concerning Multinational Enterprises *(MNEs)* and Social Policy, the Organisation for Economic Co-operation and Development Guidelines for MNEs, and the UN Global Compact;
- Cooperation with Member States – a group of high-level national representatives on CSR; and
- European Alliance for CSR – a political umbrella for new or existing CSR initiatives by large companies, SMEs, and their stakeholders.[22]

The European Alliance *(Alliance)* is an example of the implicit reach of the 2006 communication to the industry. The Alliance was formed as an industry initiative in the same year with strong backing from the European Commission. The Alliance aims to harness the resources of industry and its stakeholders thereby promoting the multi-stakeholder philosophy. The more specific target of the Alliance is to support sustainable development, economic growth, and job creation. The Alliance includes three business organisations, which are already active in promoting CSR in Europe: CSR Europe; BUSINESSEUROPE, an association of business federations; and the European Association of Craft, Small and Medium-sized Enterprises *(UEAPME)*.[23]

At the request of the European Commission, various members of industry founded CSR Europe in 1995.[24] It was established as a network with a membership that includes seventy-five multinational corporations and twenty-seven national partner organisations.[25] Thus, an umbrella perspective of the Alliance continues throughout its membership. CSR Europe, in turn, has many national organisations as members and reaches the SMEs that form the core target for the European Commission. CSR Europe's objective is to facilitate a sharing of best practices on CSR. One of the chosen methods for sharing best practices includes running projects for the industry and its stakeholders, where focus is kept on the twin objects of maintaining competitiveness and sustainability.[26] Corporate social responsibility also forms a core part of the Enterprise 2020 initiative of CSR Europe with a view to defining optimal business models for the near future.[27]

In summary, the EU agenda on CSR, as outlined by the European Council in 2001 and filled out by the European Commission in 2006, has one main objective: to support the implementation of CSR by the European industry. Because SMEs constitute the predominant form of industry in Europe, CSR in SMEs is a core priority for the European Commission. At the same time, there are on-going efforts aimed at eliminating the apparent dilemma between CSR and competitiveness by underlining the advantages for competitiveness that may result from a correct implementation of CSR. According to the Directorate General for Enterprise and Industry of the European Commission, the advent of the current economic crisis has only made CSR more important in countering the implications of the crisis.[28] In order to make the initiative more efficient, its implementation has been focused on three industry sectors: chemicals, textiles, and construction.

One of the aspects of CSR that has recently come into focus is human rights in business. The change is not intended to create new sets of rights but to facilitate the correct application and respect for human rights in business operations. The underlying intention is to achieve legal certainty and access to justice for both individuals and industry. As a reflection of the importance of this aspect of CSR, the UN in 2005 appointed Professor John G. Ruggie as Special Representative to the Secretary General on issues concerning business and human rights. In 2008, Professor Ruggie submitted a report on the issue.[29] In 2009, the European Commission initiated a follow-up study of the legal framework on human rights and the environment applicable to European enterprises operating outside the EU.[30] Concurrently, the UN Global Compact, Global Reporting Initiative, and Realising Rights published a new guide on CSR and human rights in 2009.[31]

Currently, the European Commission has issued a handbook with practical guidelines for SME's in relation to the application of CSR.[32] Likewise, an introductory guide to human rights in relation to CSR has been prepared for SMEs.[33] These handbooks do not present any new legislative or political initiatives, but build on the principles that have been developed over the preceding years.

However, in 2011 the Commission issued the results of a study on the reporting of CSR practices.[34] The study looked at how companies report and the challenges in reporting, the extent to which companies' reporting practices match readers' needs, and what public policy instruments are available to stimulate reporting. The main conclusion of the study is that due consideration of CSR is best ensured when reporting is regulated and integrated with financial reporting, and when stakeholders are more involved in reporting.

In line with the outcome of the study, the Commission has in 2013 proposed amendments to existing accounting legislation in order to improve the transparency of companies with more than 500 employees in relation to social and environmental matters. Companies concerned will need to disclose information on policies, risks and results as regards environmental matters, social and employee-related aspects, respect for human rights, anti-corruption and bribery issues, and diversity on the boards of directors.[35]

Thus, at the EU level an important step is currently being taken away from the purely supportive function of common CSR principles towards the legislative imposition of specific CSR obligations on the industry. As set out above, the issue of legal basis and the possible reach of such CSR legislative initiatives may be discussed, but current proposal, closely linked to existing accounting legislation, would seem to fall clearly within EU competence.

Implementation in Denmark

In Denmark, the Danish Ministry of Economic and Business Affairs, acting through the Danish Commerce and Companies Agency *(DCCA)*, undertakes the public administration of CSR.[36] In 2007, the DCCA established the Danish Government Centre for CSR *(Centre)*.[37] This was a follow-up to the establishment of the Copenhagen Centre in 1998.[38] The Centre functions also as the secretariat for the National Network of Business Leaders, and, in this connection, it is a member of the European Academy of Business in Society *(EABis)*.

These developments may be seen as following the European Commission policies of supporting industry initiatives and facilitating networks, while involving all stakeholders. However, a new initiative evolved in 2008 to underpin the voluntary implementation of CSR with certain legislative measures. This was based on a government Action Plan for Corporate Social Responsibility adopted earlier in 2008.[39] The legislative initiative was in the form of an amendment to the existing law on Annual Reports.[40] The amendment has since been incorporated into the law by means of a consolidated law.[41] This is a normal procedure in Denmark, so as to make the consolidated law the official legal reference. Since the Treaty of Amsterdam in 1997, it is also slowly becoming a custom within the EU.

It is clear from the preparatory work that the purpose of this Danish initiative was to encourage industry to take an active position on the issue of CSR.[42] As such, it would seem to focus on different targets than the EU because of its concentration on larger companies rather than SMEs. However, this would appear to be a distinction creating little difference because, by EU standards, most Danish companies may be considered SMEs. In designing tools for promoting CSR, it is also clear that it is SMEs that are the target of the Danish government.[43]

The core obligation of the law relates to the management report, which is part of the annual accounts. This law stipulates that any management report must specify whether the company applies a code of corporate governance, and in such case, where that code is publicly available.[44] However, this only applies to companies that have securities admitted to trading on a regulated market in an EU or European Economic Area *(EEA)* country[45] and who are required to submit such a report under Danish law. For companies that do not have securities admitted to trading, the obligation only applies to state-owned companies.[46] For all companies covered that do not apply a codex, the companies are obliged to make a statement on how they otherwise administer corporate governance. However, corporate governance is a broader concept than CSR, which is dealt with specifically in another provision of the law that applies only to large companies.[47] But, as set out below, this applies to companies that either have securities traded or are state-owned.[48] The concept of CSR is defined in the law as follows: "[C]orporate social responsibility means that companies voluntarily *integrate areas such as human rights, social conditions, environmental and climatic conditions as well as fighting corruption* in their business strategy and business activities."[49]

As for corporate governance, the law also imposes an obligation on companies that do not have a CSR policy because it requires a lack of CSR policy to be disclosed in its management report. This creates an element of pressure because a company's lack of a CSR policy can only be seen as bad for public relations.[50] The qualification as a large company, to which the CSR statement obligations apply, is a general concept used for other purposes in the law. It is generally defined in the opening articles of the Consolidated Law.[51] The definition is quite simple: large companies are those that are not small or medium.[52] In turn, small and medium companies have more specific definitions. The definition is based on three thresholds. A company is considered small or medium if it does not exceed any two of the three thresholds for two consecutive years.[53] It may, however, exceed any one of the three thresholds.[54]

The three thresholds for medium size companies are *(small size thresholds added in parentheses):*

1) balance sheet total of 143 million DKK *(36 million DKK);*
2) net turnover of 286 million DKK *(72 million DKK);* and

3) average number of full-time employees during the financial year of 250 *(50 employees)*.[55]

In addition to large companies, the obligation to make CSR statements also applies to companies included in accounting class D.[56] This concept is defined in the opening articles as a state-owned company or one that has securities traded on an EU or EEA market.[57] However, the obligation to make CSR statements in the management report is not absolute but is subject to exemptions and legal conditions. Thus, a company that has submitted a progress report in connection with the UN Global Compact or UN Principles for Responsible Investment does not need to make a CSR statement but will have to state in its management report that it has availed itself of this exemption.[58] For companies in a group with consolidated accounts, it is sufficient that a CSR statement is made for the group as a whole.[59] A subsidiary within a group may choose not to make a CSR statement if the parent company has either made such statement or availed itself of the UN progress report exemption.[60] A subsidiary company is not obligated to make any statement if it uses of this option.

While no listing of companies exists, an estimated total of 1,100 companies are covered by the obligation to make CSR statements.[61] The law provides that a CSR statement must indicate the following:

1) the *company's policies on social responsibility,* including any standards, guidelines or principles for community responsibility, which it uses;
2) *how the company translates its policies* of social responsibility into action, including any systems or procedures evidence; and
3) *the company's assessment of what has been achieved* as a result of its work with community responsibility in the financial year, and the company's expectations for any future work.[62]

Furthermore, the Danish legislative system applies a system of delegation of powers similar to the EU, where the Council of Ministers and the European Parliament may delegate to the European Commission the power to adopt implementing measures.[63] In Denmark, such powers are normally granted to the ministers concerned, who may then adopt executive orders.

In 2009, the Minister for Economic and Business Affairs issued an executive order under the amended law, which regulates the publication of CSR statements on websites as an alternative to including them in the management report.[64] One advantage for companies choosing this option is easier website updating, as opposed to the yearly management reports. The CSR statement may also be made in a separate document, to which reference is made in the management report.[65] This option applies, in relation to CSR, to companies covered by accounting class C, as well as companies covered by accounting class D of the consolidated law. The opening provisions state that medium and large companies are at least subject to accounting class C.[66] The scope of class D is explained above.[67] In this circuitous manner, apparently all companies with a CSR statement obligation may avail themselves of the web publication option. However, those using this alternative must expressly mention within the management report that they have chosen this option and they must include the Internet address where the CSR statement can be found.[68]

Finally, the consolidated law specifies the audit obligations in relation to the corporate governance and CSR statements. As a point of departure, the management report is not

subject to audit on its own, but the auditor must confirm that the report is in accordance with its annual accounts.[69] More explicitly, the executive order stipulates that the corporate government statement, on application of any code, is not subject to audit, unless it has been agreed between the company and the auditor that it should be included.[70] Again, this provision must be viewed as an effort to promote transparency by pointing towards such audit agreements.

In relation to CSR, however, the executive order does stipulate a general obligation for the auditor to actually verify that the required statement has been made in the management report or that the website has been correctly identified and labelled.[71] In relation to updating the website, the executive order makes clear that while such updates are acceptable, they must be clearly separated from the original information posted to qualify as an alternative to inclusion in the management report.[72]

Currently, the Danish government is implementing an action plan for 2012-2015.[73] The action plan aims at promoting CSR and helping Danish businesses reap more benefits from being at the global vanguard of CSR. At the same time, the plan aims at strengthening the efforts to ensure that Denmark and Danish businesses are generally associated with responsible growth.

The action plan focuses on business-driven CSR and internationally recognised principles, in accordance with the UN Global Compact and the Principles for Responsible Investment *(PRI)*.[74]

The action plan contains a total of 42 initiatives in four key areas:

- Strengthening the respect for international principles
- Increasing responsible growth through partnerships
- Increasing transparency
- Using the public sector to promote a good framework for responsible growth

Overall, the action plan may be seen as a continued support for previous initiatives, and at the political level as a basis for taking further initiatives, such as in relation to the increasing of transparency at the international level, but it does not in itself present to mechanisms to be implemented in Denmark and instead relies on the previously introduced reporting obligations, which are to promote enterprise focus on CRS obligations.

Conclusions

Currently, there is no clear basis for the EU to regulate CSR by legislative measures, as it does not form a part of the powers expressly delegated to the EU in the treaties on the EU. However, it may be argued that an interpretation of the delegated powers in relation to the internal market would allow for such legislative measures, so that actual legislation may in future support the previous strategy based on supportive measures for the industry to develop and apply CSR norms.

The Danish government has also followed this strategy by setting up public institutions with the specific purpose of supporting the development of CSR. Separately, the Danish government has mandated an element of transparency by requiring companies to

publicise their position on CSR in their management reports that form part of the annual accounts. As annual accounting is to a large extent harmonised at the EU level, this is also the platform chosen by the European Commission in order to introduce similar transparency obligations to be adopted as part of EU law.

Footnotes:

[1] See Communication from the Commission Concerning Corporate Social Responsibility: A Business Contribution to Sustainable Development, at 6, COM (2002) 347 final (2 July 2002).

[2] See, e.g., Trine Beckett, Madame CSR, Djøfbladet, The Magazine for Members of the Lawyers & Economists Trade Union in Denmark, Djøf Sheet No. 12, 23 June 2010, available at http://www.djoef.dk/djoefbladet/Arkiv/DJOeFBladet2010/DJ-OE-F-Bladet-nr-12-2010/Madame-CSR.aspx.

[3] Consolidated Version of the Treaty on the Functioning of the European Union Article 4, 5 September 2008, O.J. (C 115) 47 [hereinafter TFEU]; see also id. Articles 2-6 (specifying the areas and competences in more detail).

[4] Id. Article 2

[5] See id. Article 352

[6] "See, e.g., Opinion 2/94, Accession by the Community to the European Convention for the Protection of Human Rights and Fundamental Freedoms, 1996 E.C.R. I-1763

[7] TFEU, supra note 4, Article 6(b)

[8] Id. Article 4(2)(a)

[9] Case 43/75, Defrenne v. SA Belge de Navigation Aerienne (SABENA), 1976 E.C.R. 455

[10] Case 299/86, Commission vs. Drexl, 1988 E.C.R. 1213

[11] See TFEU, supra note 4, Article 15

[12] Presidency Conclusions, Lisbon European Council (23-24 March 2000), available at http://www.europarl.europa.eu/summits/lis1_en.htm (last visited 12 May 2013) (emphasis added)

[13] Commission Green Paper on Promoting a European Framework for Corporate Social Responsibility, at 7, COM (2001) 366 final (18 July 2001)

[14] Id. at 25 (emphasis added)

[15] Id. (emphasis added)

[16] See generally Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee - Implementing the Partnership for Growth and Jobs: Making Europe a Pole of Excellence on Corporate Social Responsibility, COM (2006) 136 final (22 March 2006)

[17] Id. at 4 (emphasis added)

[18] Id. (emphasis added)

[19] See Report from the European Expert Group on Corporate Social Responsibility & Small and Medium-sized Enterprises, Opportunity and Responsibility - How to Help More Small Businesses to Integrate Social and Environmental Issues into What They Do, (May 2007), available at http://ec.europa.eu/enterprise/policies/sustainable-business/corporate-social-responsibility/sme/european-expert-group/index_en.htm (last visited 12 May 2013)

[20] Id. at para. 6-10 & 15

[21] See TFEU, supra note 4, Article 4

[22] See generally Commission Decision Setting up a High Level Group on Competitiveness, Energy and the Environment, 2006 O.J. (L 36) 43 (EC). Find subsequent reports of the High Level Group on Competitiveness, Energy and the Environment at: http://ec.europa.eu/enterprise/policies/sustainable-business/documents/high-level-group/index_en.htm (last visited 12 May 2013)

[23] See What is the Alliance?, CSR Europe, http://www.csreurope.org/pages/en/aboutalliance.html (last visited May. 12, 2013)

[24] About CSR Europe, CSR Europe, http://www.csreurope.org/pages/en/about_us.html (last visited 12 May 2013)

[25] The European Network on CSR - Driving Change, CSR Europe, (2006), http://www.csreurope.org/data/files/csr_europe_npo_brochure_2006.pdf (last visited 12 May 2013); see also CSR Europe - Working with You (2009 – 2010), CSR Europe, (Jan. 2009), http://www.csreurope.org/data/files/csr_europe__working_with_you_20092010.pdf (last visited 12 May 2013); A Guide to CSR in Europe - Country Insights by CSR Europe's National Partner Organisations, CSR Europe, (Oct. 2009), http://www.csreurope.org/data/files/20091012_a_guide_to_csr_in_europe_final.pdf (last visited 12 May 2013)

[26] European Competitiveness Report, at 106, COM (2008) 774 final (Nov. 28, 2008)

[27] See http://www.csreurope.org/pages/en/enterprise2020.html (last visited 12 May 2013)

[28] See Günter Verheugen, Vice-President, European Commission Responsible for Enterprise & Industry, Corporate Social Responsibility Essential for Public Trust in Business (Feb. 10, 2009), available at http://europa.eu/rapid/pressReleasesAction.do?reference=SPEECH/09/53&format=PDF&aged=0&language=EN&guiLanguage=en (last visited 12 May 2013); see also Lene Espersen, CSR in a Time of Crisis, CSRgov.dk (Mar. 31, 2009), http://blog.csrgov.dk/?p=3 (last visited 12 May 2013)

[29] See Report of the Special Representative of the Secretary General on the Issue of Human Rights and Transnational Corporations and Other Business Enterprises, U.N. Human Rights Council, 8th Sess., U.N. Doc. A/HRC/8/5 (7 April 2008) (by John Ruggie)

[30] See European Commission, Enter. & Indus. Directorate-Gen., Study of the Legal Framework on Human Rights and the Environment Applicable to European Enterprises Operating Outside the EU, ENTR/09/45, 2009 O.J. (S 131)

[31] See U.N. Global Compact et al., A Resource Guide to Corporate Human Rights Reporting (2009), available at https://www.globalreporting.org/resourcelibrary/A-Resource-Guide-to-Corporate-Human-Rights-Reporting.pdf (last visited 12 May 2013)

[32] CSR handbook for small business advisers, available at http://ec.europa.eu/enterprise/policies/sustainable-business/files/csr-sme/

tips-tricks-csr-sme-advisors_en.pdf (last visited 12 May 2013)

[33] *Introductory guide to human rights for SMEs, available at http://ec.europa.eu/enterprise/policies/sustainable-business/files/csr-sme/human-rights-sme-guide-final_en.pdf (last visited 12 May 2013)*

[34] *The State of Play in Sustainability Reporting in the European Union, available at http://ec.europa.eu/social/BlobServlet?docId=6727&langId=en (last visited 12 May 2013)*

[35] *See http://europa.eu/rapid/press-release_IP-13-330_en.htm (last visited 12 May 2013)*

[36] *Corporate Social Responsibility, Danish Commerce and Companies Agency, available in Danish at http://www.erhvervsstyrelsen.dk/samfundsansvar_1 (last visited 12 May 2013)*

[37] *The Danish Commerce and Companies Agency for Corporate Social Responsibility, CSRgov.dk, http://www.csrgov.dk/ (last visited 12 May 2013)*

[38] *The Copenhagen Centre, csr-directory.net, http://csr-news.net/directory/the-copenhagen-centre (last visited 12 May 2013)*

[39] *Action Plan for Corporate Social Responsibility, CSRgov.dk, previously published at http://www.csrgov.dk/sw49167.asp (no longer present, last visited 12 January 2011)*

[40] *Amendment of the Financial Statements Act, Act No. 1403 (2008), available at https://www.retsinformation.dk/Forms/R0710.aspx?id=122862 (last visited 12 May 2013)*

[41] *Annual Accounts Act - Consolidated Act No. 323 (201), as most recently amended by Act No. 1383 (2012), available at https://www.retsinformation.dk/Forms/R0710.aspx?id=136726 [hereinafter Consolidated Act]*

[42] *See Legislative proposal for Amendment of the Financial Statements Act. 1 LF 5 (2008) available at https://www.retsinformation.dk/Forms/R0710.aspx?id=121611 (last visited 12 May 2013); see also Danish Commerce and Companies Agency, Reporting on Corporate Social Responsibility - An Introduction for Supervisory & Executive Boards (2009)*

[43] *New CSR Tool Launched, CSRgov.dk, previously published at http://www.csrgov.dk/sw58189.asp (no longer present, last visited 19 January 2011)*

[44] *Consolidated Act, supra note 37, § 107(b)*

[45] *Iceland, Lichtenstein, and Norway are included as part of the EEA.*

[46] *Id. § 107(c)*

[47] *See Id. § 99*

[48] *Id. § 102*

[49] *Id. § 99(a) (emphasis added)*

[50] *Statutory Requirements on Reporting CSR, CSRgov.dk, previously published at http://www.csrgov.dk/sw51190.asp (no longer present, last visited 19 January 2011)*

[51] *Consolidated Act, supra note 37, § 7, ¶ 2(3)*

[52] *Id. § 7, ¶ 2*

[53] *Id. § 4*

[54] *Id. § 7*

[55] *Id.*

[56] *Id. § 102*

[57] *Id. § 7, ¶ 4*

[58] *Id. § 99(a), ¶ 7*

[59] *Id. § 99(a), ¶ 5*

[60] *Id. § 99(a), ¶ 6*

[61] *FAQ, CSRgov.dk, previously published at http://www.csrgov.dk/sw51582.asp (no longer present, last visited 12 January 2011).*

[62] *Consolidated Act, supra note 37, § 99(a), ¶ 2*

[63] *TFEU, supra note 4, Article 290*

[64] *Notice for Disclosure of Corporate Governance Statement and Explanation of Corporate Social Responsibility on the Company Website, Executive Order No. 761 (2009), available at https://www.retsinformation.dk/Forms/R0710.aspx?id=126096 (last visited 12 May 2013) [hereinafter Executive Order]*

[65] *Id. Article 18*

[66] *Consolidated Act, supra note 37, § 7, ¶ 1.3*

[67] *Id. § 102*

[68] *Executive Order, supra note 60, Article 10.1-2*

[69] *Consolidated Act, supra note 37, § 135, ¶ 5*

[70] *Executive Order, supra note 60, Article 3.4*

[71] *Id. Articles 16-17*

[72] *Id. Article 15*

[73] *Responsible Growth - Action Plan for Corporate Social Responsibility 2012-2015, available at http://csrgov.dk/file/318420/uk_responsible_growth_2012.pdf (last visited 12 May 2013)*

[74] *See http://www.unpri.org/ (last visited 12 May 2013)*

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Actor

The Collins English dictionary defines an actor as ‘a person who acts in a play, film, broadcast, etc.’ or ‘a person who puts on a false manner in order to deceive others *(often in the phrase bad actor)’.* However, in EU usage, ‘actors’ are often simply ‘the people and/or organisations involved in doing something’. As this meaning is also found in US English, it also occurs in some sectors of international relations *(as in the phrase ‘state actors’, for example).* However, ‘actor’ is not normally used in this way, either in the United Kingdom or in Ireland and is best avoided. Research in the UK shows that, in this meaning, it is either not understood by the general public or, where understood, is perceived as ‘a poor translation’. In the second example below, respondents understood the ‘actors’ in question to be internationally known film stars.

Example

‘Municiplalities represent a major actor of the required change, thus their initiatives like the Covenant of Mayors should be further strengthened5 .’ ‘[The European Parliament] ... acknowledges and welcomes the success of state-building efforts by Palestinian President Mahmoud Abbas and Prime Minister Salam Fayyad, which have been supported by the EU and endorsed by various international actors.”

Giani G. Pandey
- Member

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A Royal Procession: Belgian International Non-Profit Organisations

Brussels is increasingly the Washington DC of Europe. The capital of diplomats, lobbyists and interest groups relies on Belgian corporate structures to house the myriad trade associations and interest groups seeking to monitor and influence EU decision making. Is the Belgian International Non-Profit Organisation the best vehicle for you? This article looks into certain elements which may help you decide your next step.

1. Introduction

Brussels is the headquarters of numerous European and international institutions such as the European Commission, the Council of the European Union, the European Council, an ever-expanding list of European agencies such as the European Defence Agency or the European Anti-Fraud Office (OLAF), a large *de facto* presence of the European Parliament, NATO headquarters, Eurocontrol and the World Customs Organisation.

According to figures cited in a 2011 study by the Brussels-Europe Liaison Office[1], there are 285 diplomatic missions in Brussels with 5244 foreign diplomats[2]. Brussels has an estimated 15,000 tot 20,000 lobbyists and according to some sources “100,000 experts representing public or private interests”[3].

Few will deny that the Brussels-based interest groups and associations are a key feature of the EU and international political and regulatory landscape in Brussels. Even though

the financial crisis may have put pressure for a significant number of them on their revenue streams, the financial crisis will have forced them to increase their participation in the political and regulatory processes to defend and enhance their members' interests. However, despite the financial crunch, if we are to believe the figures of the 2013 survey conducted by the Belgian-based Federation of European and International Associations (FAIB), with an estimated annual income of 2.9 billion Euro, the approximately 2265 EU-focused associations based in the Brussels area are still big business. Of these associations approximately 1600 entities are EU trade associations representing business. The size of the entities varies from the small and quasi dormant entities to the large and intensively active associations, depending on who they represent, the sector they are in and the extent to which there are issues of concern to their members.

The majority of the EU trade associations are incorporated as International Non-Profit Organisations (in Dutch Internationale Vereniging Zonder Winst, or IVZW and in French Association Internationale Sans But Lucratif or AISBL).

2. Historic background of the International Non-Profit Organisation in Belgium

The two main types of Non-Profit Organisation in Belgium are the Non-Profit Organisation and the *International* Non-Profit Organisation.

The International Non-Profit Organisation is the oldest of the two forms. In 1919 the Belgian legislature passed the Law of 25 October 1919 enabling the creation by Royal Decree of International Non-Profit Organisations with their own legal personality[4] National Non-Profit Organisations with their own legal personality were as such not yet possible then.

Since its independence in the 19th century, Belgium had been the host of many new ideas which were approached with reluctance elsewhere. As such many international movements and associations held congresses at the end of the nineteenth century in Brussels. This lead the Belgian legislators to adopt a new separate legal structure which would allow the entities to function in Belgium and at the same time keep their international character. The new legal entity was given a very wide discretion as to how it organises itself internally so that it could mirror the foreign internal structures and *modi operandi* it was used to in the countries of origin.

The fact that, contrary to other legal entities, the King of Belgium uniquely grants legal personality to the International Non-Profit Organisation by Royal Decree, enhancing thus the prestige and image of the entity, is in itself too a non-negligible element reflecting the state of mind of the then legislature towards the international associations.

3. Characteristics of the International Non-Profit Organisation

a) Objective:

The *International Non-Profit Organisation* must be incorporated with as its objective *"to pursue a non-profit purpose of international use"* excluding "commercial and trade activities" and *"not seeking to provide material benefits to its members"*.[5]

The objective must be clearly defined in its statutes and it is not allowed to act outside of the stated statutory objectives. Where it does, the directors can be held liable.

If the statutes contain provisions which indicate that it will be acting as a commercial entity, the Ministry of Justice who is responsible for reviewing the statutes will not approve the statutes.

The jurisprudence has further clarified that the stated prohibition to have commercial and trade activities should be understood as meaning that commercial activities can not be the primary activity. The situation for International and national Non-Profit Organisations is in this respect identical.

As such International and National Non-Profit Organisations can, and in practice often do, carry out significant profit-making activities. These will often include obtaining revenue through research projects, publications, seminars and conferences, or even having shares in commercial companies.

The Belgian Supreme Court has clarified that firstly these revenue-generating activities can only be carried out on an ancillary basis as opposed to its main non-profit making activity. Secondly there must be an intrinsic link between the revenue-generating activity and the primary non-profit objective. The revenue-generating activity must be useful for the achievement of the primary objective. Finally, and crucially, the revenues must be allocated to the primary objective.

The profits may thus not be redistributed to the members as would be the case with shareholders in a classical commercial company.

This does not mean though that the revenues may not per se somehow benefit the members. It is thus perfectly legitimate for the association to dedicate its resources to promote the interests of its members through lobbying activities. However, if the entity were to be dissolved, then the assets will have to be allocated to another non-profit entity.

The international element is obviously one of the key distinguishing elements between the International and National Non-Profit Organisations. As regards to the international element of the objectives of the International Non-Profit Organisation, in practical terms this means that the achievement of its purpose must potentially be useful beyond the Belgian territorial scope. Activities in respect of the European or international institutions, even if they are based in Brussels, would certainly qualify for complying with the international element.

b) Membership:

Membership in International Non-Profit Organisations must be open to both Belgian and non-Belgians. Membership criteria are allowed but must be objective and not contain prohibited discriminatory provisions.

A significant advantage for trade associations seeking discretion of their membership was that contrary to National Non-Profit Organisations, International Non-Profit Organisations did not and still do not have to disclose their membership

list. Since 2009 National Non-Profit Organisations no longer have to publicly disclose their membership list either. Currently then for both the International and National Non-Profit Organisations only the founding members are publicly identifiable, unless the association of course voluntarily discloses the membership.

c) Obtaining legal personality by Royal Decree:
As mentioned, contrary to other legal entities such as the National Non-Profit Organisation, the International Non-Profit Organisation obtains legal personality by Royal Decree. Once the statutes have been drafted , a notary deed will to that effect have to be deposited at the Ministry of Justice who will review the statutes.
Whereas the Royal Decree process does create as a potential benefit the perceived enhanced status as opposed to other legal entities, it does also delay the incorporation process. One should thus foresee a three-month waiting period post submission of the notary deed, though in practice timeframes may differ on a case by case basis.

Although by contrast the complete incorporation process for a National Non-Profit Organisation could in theory be done within a week, the timing element is in practice only a minor inconvenience. Pending the granting of the Royal Decree, the International Non-Profit Organisation can already be quasi fully active as an entity in the process of incorporation.

d) Liability of Responsibility:
As a result of obtaining its own legal personality, the International Non-Profit Organisation, as is the case with the National Non-Profit Organisation, the members do not incur liability for the activities of the association.

e) Registered seat:
The official registered seat must be in Belgium, but it is can also have an additional presence in other jurisdictions.

f) Language:
The official language of the association will depend on the precise location of the entity. In Brussels the official language may be either or both French and Dutch. In Brussels official communications with the national authorities will have to be in one of these two languages. However, the association may choose another language for its internal activities or communications with third parties such as the EU and international institutions.

g) Corporate structure:
As mentioned already, the Belgian legislature has historically chosen to grant the International Non-Profit Organisation a very wide discretion as to how it organises itself internally so that it could mirror the foreign internal structures and *modi operandi* it was used to in the countries of origin.

The International Non-Profit Organisation can be set up with a minimum of two members, unlike a National Non-Profit Organisation which requires at least three members.

As to the decision-making organs, the legislature only requires a minimum of two bodies, a directional body and a management body, without going much further in

setting out the precise decision making powers and procedures.

By contrast these elements have been more regulated for the National Non-Profit Organisations.

In practice it is thus not uncommon that the founding members will either copy their foreign decision-making procedures and structures into the International Non-Profit Organisation, or copy these from the legal provisions of the National Non-Profit Organisation, or pick and choose from these two routes.

h) Tax regime:
National and International Non-Profit Organisations are in principle not subject to Belgian corporate tax. However, they may be subject to Belgian VAT for some of their commercial activities.

i) Accountancy obligations:
All National and International Non-Profit Organisations must submit their accounts to the authorities on an annual basis and they must be kept in accordance with the applicable Belgian accountancy legislation.

j) Employment law:
National and International Non-Profit Organisations are not obliged to have employees. If they do, then the employees will in principle be subject to Belgian employment law. Two issues which must be dealt with carefully in practice are employee rights in cases of dismissal and how to best structure remuneration payments in a country with very high employer tax and social security contributions.

4. What about the *de facto* association?

Interest groups, companies and individuals can in principle create a *de facto* association without practically any formalities other than a mutual understanding. As such the obvious advantages are the speed of formation and the low if any formation cost.

The de facto association can have its own name, but it does not have its own legal personality. As a consequence it does not have to submit its own annual accounts to the authorities or file its own income tax declaration.

The reverse side of the medal is however that it can not own its own assets, nor file any legal challenges or defences on its own behalf. In effect it is a collection of the individual members, without any separation of liability.

As such, whereas the *de facto* association can for some activities indeed be a perfectly workable solution, for the potential founders of active trade associations the lack of separate legal personality with linked disadvantages will often outweigh the immediate perceivable advantages.

5. What about anti-trust compliance?

EU and national anti-trust rules apply regardless of the chosen legal structure. Any venue

where potential competitors meet is a potential risk scenario which must be addressed with necessary pro-active and reactive care.

Each trade association should have its own active and regularly updated antitrust compliance program tailored to its structure, activities and types of members. Especially in an environment where people meet from potentially very different legal and business cultural backgrounds, members should be provided with clear instructions as to what is and is not permissible when meeting both within and outside of the trade association given the risk of cross contamination of a cartel infringement. Under current EU competition law, any act which may be perceived as a potential anti-trust infringement within or in the context of a trade association requires the other members and the association to react immediately and sufficiently strongly against it.

6. Conclusion

As set out above, potential trade associations or companies wishing to monitor and contribute to the regulatory environment they or their members are impacted by have a number of options from which to choose, each which their respective advantages and disadvantages.

An article in the New York Times entitled *"Lobbying Bonanza as Firms Try to Influence European Union"*[6] paints a realistic yet incomplete picture of the current EU lobbying landscape in Brussels. The article sets out anecdotally the advantages Brussels- based law firms have, as opposed to lobbyists or trade associations, because of the law firms' often close professional and personal contacts with the EU institutions and the legal privilege and non-disclosure obligations lawyers benefit from.[7] However, the article fails to paint the more complete picture that often, rather than merely acting as competitors, some EU regulatory law firms do work closely and efficiently together with lobbyists and the various types of trade associations to obtain the best possible outcome for all involved.

Just as being able to show demonstrable added value for membership,[8] robust leadership from the association management, developing a proactive public affairs department, establishing a smooth financial administration, being able to chose the most appropriate legal vehicle and ensuring subsequently legal compliance are equally key success factors for trade associations. Each factor element is to be reviewed with care but always with the larger picture in mind and the potential impact on the other factors, or as some might state more elegantly, "True wisdom comes from seeing the unity in the diversity…".

Footnotes:

[1] "Brussels – Europe the figures. A study by the Brussels-Europe Liaison Office", November 2011.

[2] Figures excluding Belgian diplomats.

[3] "Will the real lobbyist please stand up", The Bulletin, 12 October 2011.

[4] The Law of 25 October 1919 was repealed by the Law of 2 May 2002. The legal structure was as a result incorporated into the Law of 27 June 1921.

[5] Article 46 of the Law of 27 June 1921.

[6] "Lobbying Bonanza as Firms Try to Influence European Union", The New York Times, 18 October 2013.

[7] The Belgian legislation and the professional conduct rules for Belgian registered lawyers grants a very high level of protection to the communications and work carried out by lawyers who are member of a Belgian Bar.

[8] "Key success factors for European associations," Ellwood Atfield report, 2013.

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Modality

‘Modality’ is one of those words which people (a) swear is correct and (b) say they have to use because the Commission does so (the example below is a case in point). The trouble is that it is not English – at least not in the meaning applied in our [EU] texts.

Example

‘Evaluating such a unique scheme is a particular challenge for all actors involved. Evaluation modalities have gone through significant changes over recent years.'

Davide Rovetta

- Of Counsel

Davide Rovetta is an Italian trial attorney (Avvocato) with substantial experience advising and representing clients in commercial, customs and trade related matters in Italy and EU and non-EU countries. In addition he has wide experience related to arbitration in commercial, investment and public international law matters. He has appeared on a number of occasions as a member of a sovereign WTO Member delegation before WTO Panels and the Appellate Body as well as before tax, customs, criminal and civil Courts and Tribunals. Davide has published widely on EU customs, trade law, arbitration and WTO issues.

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Multi-Jurisdictional Legal Privilege Issues in Internal Investigations Related to Trade, Sanctions, Anti-Bribery or Embargo Matters

Often following to checks by the EU national authorities during trade, sanctions, anti-bribery or embargoes matters companies have to provide such authorities with exculpatory evidence or pleading not guilty. In turn, it is not rare that in such situation the governing bodies of such companies order an internal investigation to take place to understand what has happened.

However those companies that have headquarter outside the EU, like for instance in the US, have the need to coordinate such defensive actions vis a vis the EU authorities and internal investigations with such headquarters. Similar issues arises concerning companies that have branches in third countries like for instance Africa.

The article will examine how to make sure that coordination of the defensive actions between branches in different EU and non-EU member states with headquarter is covered by legal privilege, what kind of problems of legal privilege can arises in such situations as well as how to minimise the risk that any negative finding in the internal investigation is used by the EU national authorities against the company at issue.

1. Introduction

Following up on spot checks by the national authorities of EU Member States, it often happens that companies discover misbehaviour on the part of their employees or management. For instance, it might happen during investigation of customs matters that an employer discovers employees in a local branch in a given EU Member State have supplied the customs authorities with false certificates of origin to obtain favourable tariff treatment. Even worse, a company may discover that such employees have perhaps engaged in illegal activities and paid bribes to foreign extra-EU customs authorities to obtain false certificates of origin to avoid anti-dumping duties or that they have materially falsified such certificates. Employers may also happen to discover that sanctions or embargoes in force in the EU have not been respected due to incorrect choices by the management or a conspiracy by employees. Finally, it may happen that dual use legislation has not been applied correctly.

Most North American companies have branches in Europe and could be faced, sooner or later, with situations like those described above. The instinctive reaction of the average American multinational in such an instance is to immediately set up an internal investigation in order to ascertain what has happened. Once such an investigation is concluded, the company at issue usually would like to take action to put things in order. This can be done by taking employment law measures against those responsible for the wrongdoing as well as evaluating whether or not to make a disclosure to the authorities in charge.

2. The European Union is not the USA: legal privilege in the European Union

Against the above background, however, one should consider that the European Union is not the USA. The EU has in place a common double legal framework constituted by European Union law as well as by the European Convention on Human Rights. Both such legal orders are, to a different extent, controlling within the EU Member States. At the same time, in the European Union there are 28 different Member States with 28 different legal systems. Most of them are civil law continental systems. In other words, in the EU Member States there is a complex multi-level legal order which will be applicable to the above mentioned internal investigations. While EU law and the European Convention on Human Rights will always be present in all EU Member States legal orders, part of the substantive law applicable to internal investigations will vary from Member State to Member State of the EU. If the above is true in general, this is even more true concerning the law of legal privilege.

The results of internal investigations or, worse yet, the evidence collected during internal investigations, will be subject to different degrees of legal privilege, depending on the Member States in which such investigation is conducted. It is not the same to conduct an internal investigation in France as it is in Italy or Germany. At the same time, American companies often have the bad habit of letting US lawyers admitted to practice in the US only conduct internal investigations in EU Member States without local attorneys supporting them. They meet and interrogate people, access offices and premises and PCs and send out data to the US headquarters. This may result in a fatal mistake.

First of all, the majority of EU Member States' legal orders do consider that privilege laws and benefits are not applicable to those lawyers that are not admitted to practice in their jurisdiction. The UK seems to be a notable exception to this rule. As a consequence the

American lawyers or company in-house lawyers performing internal investigations in the vast majority of EU member states will not be protected by legal privilege. The same therefore will hold true concerning the documents formed and collected during the internal investigation.

At the same time the conduct of an internal investigation in such manner may result in the breach of local employment laws or, in certain selected cases, of local criminal law. Often following authorities' discovery of wrongdoing, a criminal proceeding is activated or at least prosecutors begin criminal law investigations. If at the same time as the official criminal law investigation, in-house company lawyers or external lawyers perform a concurrent internal investigation, this may result in obstruction of justice charges against them. This may occur if the internal investigation is not conducted by taking all appropriate steps to avoid interference with the investigation by the criminal law authorities. Due to cultural differences and different legal traditions it may easily happen that there are misunderstandings on such issues.

The law of privilege is controlled by the law of the Member States in which the internal investigation is performed applied in combination with the European Convention on Human Rights and, in certain circumstances, with EU law. It is often therefore very difficult, if not impossible, for a US-based attorney not familiar with the above to ascertain what the boundaries to be respected are.

Finally, often during internal investigations there are sensitive data protection and privacy issues related to the transfer of data and documents to the US. There is framework EU legislation applied in different ways at the national level by the EU Member States with different sanctions in case it is breached. Such sanctions vary from Member State to Member State and may be criminal or administrative law in nature, or both, depending where in the EU the breach takes place.

3. Conclusion

In practice situations are often even more complex than in the above examples. It often happens that an internal investigation has to be performed simultaneously or sequentially in different EU Member States. The issue that arises for the company is, therefore, how to maintain the proper protection of legal privilege laws and to make sure that "the chain of privilege" is not interrupted in a given member state ,rendering such a company vulnerable.

In order to minimise risks and to deal with such challenges, it is advisable to rely on local attorneys who are duly admitted to practice and to obtain their preventative advice first. Such advice should cover not only the legal feasibility of internal investigations in a given country but also the way of conducting it. It should also cover the way of transferring data to other EU Member States and, where appropriate, to the US without breaching data protection and privacy rules as well as maintaining to the extent possible the protection of legal privilege.

Only local attorneys will know when and to what extent privilege can be claimed and they should be familiar with all appropriate actions before the relevant Courts and Tribunals if they are needed.

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Third Country

The USA is one country, Canada is another, and Ireland is a third. The USA could sign an agreement with Canada to exclude a third country *(e.g. Ireland)* from their territorial waters *(for fishing, for example)*.

In EU texts, the term is widely used to mean ‘countries outside the European Union’, and sometimes ‘countries outside whatever grouping of countries we are talking about’. This is incorrect and largely incomprehensible to outsiders.

It is also objectively unclear.

Vincent Smith
- Of Counsel

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In addition to supporting the further development of our competition practice, Vincent also brings that most valuable of commodities: a real understanding of how national Competition Authorities think and work in the EU and a unique network of contacts. Vincent is able to provide valuable counselling, advice and support on all aspects of EU competition law.

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Cartel Recovery: How Victims of EU Cartels Can Get Their Money Back

Cartel victims are increasingly able to claim compensation for unlawful overcharges in EU courts. The European Commission and a number of national administrations now actively encourage court claims against companies which have broken competition rules - and non-EU companies can, and have, taken advantage of this. Collective claims by groups of victims are becoming more common and allow claimants to smooth the risks of making claims by grouping together with other similar claimants.

Recovery of compensation by the buyers of goods or services whose prices were inflated by unlawful cartel behaviour in the EU is on an increasing trend. Claims are also encouraged by the European Commission, and national competition authorities *(for example the OFT in the UK).* Importantly, the cartel decisions of the European Commission *(unless set aside on appeal)* are binding on the civil courts in each Member State that are empowered to hear victims' claims for compensation.

Although the EU system of *public* enforcement of competition rules is now quite centralised – with the larger cartel cases in practice being investigated by the European Commission in Brussels – claims for compensation for loss caused by cartels in the EU need to be brought to? a decentralised system, before a national civil court having jurisdiction to hear the claim.

Making a claim

Typically in a cartel case involving companies from a number of different EU Member States and which has had an effect on competition across the EU, several national courts will have jurisdiction to hear claims for compensation. Some of them are more favourable to claimants than others. But all competent courts in the EU will hear claims from potential victims of an EU cartel regardless of their nationality, subject only to their being no prohibition in the claimant's domestic law *(or in international law – eg due to sanctions)* on the claim being pursued in the EU.

This note outlines a *hypothetical* scenario for recovery of damages following on from the European Commission's findings in a European cartel decision. We have based this example on the Commission's decision in the liquid crystal display panel cartel. There are a number of actions already underway against this cartel in EU courts and this example is not intended to represent any particular one of them, but only to give an outline of how a compensation claim might begin.

The principles set out here are based largely on the practice in English law and the English courts but many of the principles have their basis in overriding EU law and will apply in a similar way across the European Union.

LCDs are the flat screens used in many TVs and, more importantly, in computer monitors and laptops. The cartel of six defendants *(mainly from South Korea and Taiwan)* was found by the European Commission to have fixed the price of LCD panels for computers and TV screens from late 2001 to early 2006 (*a 4½ year period)*. The cartel was found to have had a significant effect on competition for the customers of the cartel members, although *(as is usual)* the Commission did not quantify the size of the effect in its decision.

It is of course possible to begin a claim for compensation in a national court as a single claimant, but due to the complexities of this kind of work, claimants in a similar position often choose to join together to bring a collective claim.

There are various ways of organising the group to best advantage – and the methods of doing this do vary somewhat as between different courts and EU member States. As a rule of thumb, claimants will have a good chance of creating a viable cartel claim if they are a *group* of businesses having combined relevant *purchases* of €100 million over the whole cartel period: this would suggest a group of 15-20 members in relation to most cartel actions.

As mentioned, it is possible to start a smaller claim but this may exclude some of the funding options set out below.

Building the claim

The claimants will need to consider:

- their *representation (advisers)*, to support them in bringing the claim
- *organisation* of the claim and the evidence needed to demonstrate it
- *financing* the claim process

Representation

For an action in England the claimant group will need to employ:

- **Solicitors:** to administer the claim, advise on competition law, consider evidence and conduct settlement discussions;

- **Barrister:** specialist advocates, needed if there is a serious risk of the group's claim going to trial;

- **Expert economists:** to quantify the claim of each group member on the basis of the evidence presented;

- Depending on the state of the records, it may be necessary to use a **data search consultant** to copy and reconstruct old computer files: the hypothetical attached to this assumes that all group members keep their files in sufficient order that this service will not be needed.

In Member States other than England, legal representation is normally through an *avocat* or equivalent – the two-tier system in England is not reproduced elsewhere. Although the English system appears more cumbersome, in practice it works well as most cases of this kind are settled without trial, reducing the need for substantial barrister input at earlier stages of the case.

Organisation

The principal elements that will affect the degree of success of the group's claim are likely to be:

- how good their records are *(a data consultant may be needed to recover them in exceptional cases)*

- the relationship between the group members for the purposes of bringing the claim. It is common for this to be set out in an contract which will deal with *(among other things);*

  - how the costs of the claim will be divided up;
  - what happens if the group members disagree on how the litigation should be conducted, in particular where a settlement offer is made. In many cases, refusing a reasonable settlement offer will have consequences for the later recovery of legal costs and it is sensible for this to be factored into the agreement between the claimants as far as possible;
  - how to deal with offers of settlement which are made only to some members of the group;what happens if a group member leaves before any settlement or compensation has been achieved.

- how much in common the claims made within the group are: it is helpful to keep a group relatively focussed with similar factual characteristics to get the most benefit from a collective claim.

Financing the claim

There are currently four main methods of covering the costs of litigation *(which may be combined in some cases):*

- **own resources:** traditionally litigants paid their representatives and bore the risk of adverse costs themselves;

- **insurance**: legal expenses insurance can be taken out to cover the risk of having to pay the defendants' costs. Often this is done after the event which gave rise to the claim *(eg a cartel)* took place *(After-The-Event – ATE – insurance)*. Traditionally this was used for smaller claims *(personal injury)* but insurers are now offering polices which can cover the larger risks in complex litigation against cartels;

- **funding:** a fund takes over the risks of litigation and usually also agrees to pay the clients' own legal costs – all in return for a percentage of the clients' money recoveries. At present, for complex cartel litigation the percentages charged are usually quite high *(30-40% is not uncommon and 25% is likely to be a bottom line)*. Funders will also require a minimum claim size before they will take on a claim;

- **assignment:** a company set up to run the case 'buys' similar claims in order to pursue them in its own name – usually the price is a percentage of the expected compensation amount *(how high a percentage varies from case to case)*. This method of funding cases is not permitted in all EU courts *(for example, not in England).*

Viability of claim

There is a strong distinction between claims for compensation made using a European Commission decision as their basis – so-called 'follow-on' claims – and those where the claimant(s) have to prove the existence of the cartel *('stand-alone').* Most compensation activity in European courts is at present 'follow-on' as these claims are more viable: the public authorities have already done a large part of the work needed to prove the claimants' right to compensation.

The LCD decision by the European Commission is unusual as the cartel members entered into a settlement agreement with the authorities under which they admitted to participating in the cartel and to pay an agreed penalty lower than would have been imposed without the settlement. Although these kinds of settlements are relatively common in the US, they are still unusual in Europe.

Where the European Commission has found a cartel to exist – especially where one of more of the members of the cartel has confessed to the Commission in return for a lesser (or no) penalty as in the LCD decision – it is very unusual for a claim to go to trial. Instead the cartelists will normally wait until the public process has finished and will then be willing to settle claims, at least from the larger businesses who have bought directly from them. Often these kinds of settlements will be wholly or partially in the form of forward-looking reductions in input prices.

If the members of a cartel contest the substance of the Commission's decision, the appeal process *(to the Court of Justice in Luxembourg)* will need to be completed before

a national court can order compensation to be paid to the victims of the cartel in a follow-on action. However, national courts may nevertheless continue with pre-trial measures so that the claims can be swiftly disposed of after the Luxembourg court has given judgement.

Conclusion

The European legal system for obtaining compensation from cartelists is still evolving fast and most of the developments at the level of national courts are in favour of potential claimants. Major EU countries such as the UK and France either have made or are proposing legislation to make claiming against cartelists easier – especially for groups of claimants whose individual loss is low but who together have substantial claims.

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Elaborate

To elaborate means ‘to work out carefully or minutely’ or ‘ to develop to perfection’. It does not mean to write something up. It is possible, though rather unusual, to elaborate a strategy, but not a document.

Example

‘Additional background information on less commonly used species, and habitats is available in the background information document elaborated by the Group of Experts’.

Peter Trepte
- Of Counsel

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In the case of regulated procurement, he advises and represents public and private sector clients on the impact of the EU procurement rules as well as on the application of the WTO Agreement on Government Procurement and the effect on the procurement rules of the EU's preferential trade arrangements. He has advised a number of developing and transition countries around the world on procurement reform.

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Washing Your Dirty Laundry in Public … Procurement:

The New European Procurement Rules

"Mae'r erthygl hon yn sôn am y rheolau Ewropeaidd newydd sy'n berthnasol i eithrio cwmnïau rhag gwneud cais am gyntundebau gyda awdurdodau cyhoeddus. Mae'n dangos sut mae'r deddfwr Ewropeaidd wedi methu a gyflawni'r hyn y mae'r rheolau yn ymddangos i addo."

The European Union legislators have now all but formally agreed to the text of what will be the new procurement directives, expected to be adopted early in the New Year, if not before. Along with many other innovations, the text has considerably strengthened the probity and integrity provisions, including the introduction of new conflict of interest provisions. The most novel addition, however, is perhaps the introduction of a rehabilitation clause which would allow tenderers convicted of corruption offences to avoid debarment from participating in a procurement procedure where they can show that they have implemented effective corrective measures *(such as compliance programmes)* to redress the circumstances that gave rise to the offence and ensure that there will be no recurrence.

The EU public procurement rules are those that apply when contracting with public authorities and utility operators in Europe. They apply to relatively high value contracts for the supply of goods, construction and other services. These rules are not new and have been the subject of several changes over the years. Following a recent two year consultation phase, the European legislators have finally agreed the text of the latest iteration of the rules which were supposed to be adopted before the end of the year. They are most likely to be adopted early next year and will come into force throughout the EU by 2016. The final agreement on the text, however, means that adoption is now mostly a formality. The content of the new rules are already known.

These rules apply safeguards against discrimination on grounds of nationality for the benefit of tenderers from EU member states and do so through the application of transparent contract award procedures and objective and non-discriminatory selection and award criteria as well as technical specifications. The rules in respect of contracts let by utility operators are somewhat more flexible. One of the key features of the rules has always been the use of 'selection' criteria whereby tenderers could only be disqualified for failure to meet those selection criteria that were set out and advertised in advance. These selection criteria encompass provisions relating to the general suitability of tenderers, their economic and financial standing and their technical capacity.

The criteria relating to economic and financial standing and to technical capacity might more properly be described as 'qualification' criteria since they apply, for the most part, to the ability of tenderers to fulfil the terms of the contract, i.e. whether they are financially and technically able to perform the required contractual obligations. The criteria related to general suitability are more akin to eligibility requirements since they are not connected with the ability of the tenderers to perform the ultimate contract but with the desirability or not of the tenderer as a contracting party. Under the new rules, the scope of these eligibility requirements have been expanded and now include various integrity related criteria connected, among others, to corrupt activities.

Notwithstanding the serious consequences of the mandatory exclusion of tenderers based on bribery convictions, to date, these disqualification criteria have been drafted as if they applied to single contract award procedures, i.e. if a tenderer was found to fall into one or other of the identified categories, it could or must be excluded from the contract award procedure at issue. Whilst the rules did not exclude the possibility of national systems which applied a more rigorous and permanent debarment system *(i.e. where tenderers could be excluded for a given period of time where they fell within one of the defined categories),* they did not themselves foresee or provide for such a system. The situation under the new rules has not changed in this regard, to the extent that the rules do not provide for an EU-wide debarment system, but they do now clearly foresee the existence of such debarment systems at a national level and, to some extent, provide for a mechanism to deal with cases where a national debarment system is incomplete.

Crucially, the rules also provide for rehabilitation, a system under which tenderers can overcome disqualification or debarment by demonstrating that they have taken action to reform themselves and prevent future transgressions.

These changes establish a significantly new approach to exclusion and debarment from procurement procedures which will have far-reaching effects on tenderers bidding for contracts within the EU.

The Beginnings of an EU Debarment System

The EU rules have not until now contained any provisions which might be construed as establishing a complete system of debarment, i.e. a system under which tenderers could be prevented, either temporarily or permanently, from participating in contract award procedures based on their previous conduct. Such a system presupposes the existence of a relatively sophisticated investigative process *(including due process safeguards)* capable of assessing the severity of any offences on the part of potential tenderers and of applying various preventative measures according to the nature of the offence and the likelihood or acceptability of remedial action. Instead, the EU rules have thus far imposed a rather blunt instrument which consists in the mandatory exclusion of tenderers who have been convicted of offences related to, inter alia, corruption. The consequence is to exclude convicted tenderers permanently from participation in contract award procedures with no possibility of rehabilitating themselves. The draconian effect of exclusion, whilst arguably disproportional to some of the offences, has had a significant impact on tenderers. Under the new rules, member states are required to establish implementing mechanisms and a key feature of these must be determining the maximum period of exclusion. Where this is not fixed, the new rules set the maximum at 5 years. As a result, mandatory exclusion will no longer be permanent and will be subject to the rules' rehabilitation process and thus fall within a more broadly defined debarment system.

The additional discretionary grounds for exclusion are of less significance to the extent that they are precisely that: discretionary, i.e. they may or may not be relied upon at the discretion of the contracting authorities, although member states have the faculty of making them mandatory. There is no system in place to ensure consistency of the applicable rules; the consistency of application in all of the member states; or even their application at all. The discretionary grounds for disqualification are also seen as applying to specific contract award procedures and not generally seen as part of a broader system of debarment. The lack of an EU-wide debarment system has not prevented the legal systems of the member states from themselves operating debarment systems and, indeed, it is clear that some member states do operate such debarment systems. Germany, for example, has established debarment systems in most Federal States. In other member states, the EU exclusions have been supplemented in various ways. These member states include Austria and Italy as well as the United Kingdom which has, for example, made offences under the recent Bribery Act of 2010 discretionary grounds of exclusion.

Despite these efforts, the piecemeal approach to debarment and the lack of consistency, notably in the context of the discretionary grounds for disqualification, means that the EU has a patchwork of legal rules that apply to debarment. The new rules do not overcome these difficulties, but they do at least provide for some common ground, although it will continue to be necessary for tenderers to have regard to the laws applicable in each of the member states. The situation may now become less uncertain but it remains messy.

They Key Changes

Some of the changes made to the rules demonstrate that the EU legislator is beginning to see the exclusion rules as part of a bigger picture of debarment. Without fundamentally changing its approach at the EU level, some of the new provisions clearly allow for *(and to some extent require)* the creation at national level of more sophisticated debarment

systems. The strengthened requirement that member states must put in place laws, regulations or administrative provisions to implement the article relating to exclusion means that each member state will be obliged to establish some form of debarment system, including one which provides for maximum periods of debarment. The additional requirement to provide minimum conditions of rehabilitation also means that there will be some minimum safeguards throughout the EU. The broad parameters of such a debarment system are now discernible from the revised rules.

Apart from refining its definition of corruption under the grounds for mandatory exclusion, the position under the new rules has not fundamentally changed. However, inclusion of definitions found under national law implies that member states will need to ensure that their own national systems provide for exclusion on these grounds more comprehensively. As explained further below, the new rules also strengthen the provisions relating to the convictions of senior management which may prove problematic for tenderers having employed or intending to employ management staff with convictions that might exclude the company from tendering for public contracts.

The grounds for discretionary exclusion have been expanded and now contain further references to integrity and conflicts of interest thus broadening the potential grounds for debarment. Some of the new grounds for exclusion, such as those based on contractor performance, imply the ability to collect information regarding previous contracts with various authorities in the public sector. This presupposes the existence of a contractor registration or debarment system. Of some concern is the fact that the conditions permitting reliance on these grounds for exclusion appear to have been softened so that contracting authorities may more easily exclude tenderers based on information and evidence they possess rather than on the basis of independent findings of fact or convictions. These grounds for exclusion may also become mandatory to the extent that the new rules allow for member states to require contracting authorities to exclude tenderers where these grounds are met. This enables member states to start creating broader debarment systems, although the lack of precision in the means of proving that these conditions are met is likely to be problematic in practice and should be of significant concern to tenderers. This will be entirely dependent on the implementing measures adopted by the various member states.

The emergence of a move towards incorporating these exclusionary measures into a broader debarment system can also be seen from a number of new provisions which clearly indicate that exclusion is no longer contract specific, i.e. not based merely on the qualification criteria required to be met for the purposes of fulfilling the contract which is the subject of the contract award procedure at issue. Contracting authorities must now at any moment during the procedure exclude a tenderer where it turns out that the tenderer in question falls, in view of acts committed or omitted either before or during procedure, within one of the grounds for mandatory exclusion. In the case of the grounds for discretionary exclusion, contracting authorities may do so on the same basis *(i.e. at any time and based on facts arising before or during the procedure)*, although member states may also require them to do so *(presumably where they also make the EU's discretionary grounds for exclusion mandatory: see below)*. This again presupposes broader knowledge than would ordinarily be possessed by a contracting authority in the context of a single contract award procedure.

One of the most novel features of the new rules on exclusion concerns the introduction of rehabilitation measures *(sometimes referred to as self-cleaning measures).* This is a common feature of existing comprehensive debarment systems but is a novelty within the

EU rules, although many have argued that it should have been incorporated by analogy, if only to satisfy the EU principle of proportionality. Under the new provisions on rehabilitation, tenderers are able to offer a defence to exclusion in the form of evidence of remedial action having been taken to remedy the offences. This possibility is retrospective in the sense that the tenderer must provide evidence of what it has done, not what it will do. It is thus also an indicator of a much broader debarment system which presupposes the ability to take into account past behaviour outside the contract award procedure at issue. There is some lack of clarity in this respect, however, since the new rules also provide that rehabilitation is not available where exclusion is fixed by final judgment. This devalues the remedial effect of rehabilitation since, once the period of exclusion is over, the tenderer is in any event permitted to tender and is no longer excluded. Rehabilitation is then of little value.

Finally, under the provision requiring member state implementation of the exclusionary rules, the legislator imposes some critical minimum requirements. It requires, for example, that the national implementing rules provide for a maximum period of exclusion where no remedial measures are taken by the tenderer to demonstrate its reliability. This implies the creation of a more graduated debarment system which provides for temporary as well as permanent debarment dependent, inter alia, on the implementation and scope of remedial actions leading to rehabilitation. This cannot be done effectively outside a full debarment system. Where maximum periods of exclusion have not been set by final judgment *(suggesting again a system operated by way of third party),* the new rules provide for these maximum periods themselves: not more than five years from the date of the conviction by final judgment in the case of mandatory exclusion and not more than three years from the date of the relevant event in the case of discretionary exclusion.

Grounds for Exclusion

Whilst the general suitability criteria have always been referable to the eligibility of tenderers, since the introduction in 2004 of specific grounds for exclusion, these have been kept separate so that the ‘suitability’ of tenderers to pursue a professional activity has been treated together with the remaining financial and technical grounds for selection even if this criterion is also not directly related to performance.

The exclusionary rules are of two sorts: mandatory and discretionary, and both have been amended in the forthcoming new rules.

Mandatory Exclusion

The mandatory rules for exclusion, first introduced in 2004, are aimed at dealing with ‘dirty money’. They effectively exclude from participation any tenderer which has been convicted by final judgment for participation in a criminal organisation, corruption, fraud, terrorist offences or offences linked to terrorist activities, or *(under the new rules)* child labour and other forms of trafficking in human beings. This exclusion operates only where there has been a final conviction; it will not operate on the basis of suspicion or disciplinary action or even where the conviction is still subject to appeal.

Importantly, the provision on mandatory exclusion resulting from a conviction for corruption has been amended. The definition of corruption has now been extended from

only covering the definition contained in relevant EU acts concerning the fight against corruption involving officials of the European Communities or officials of Member States of the European Union to now including the definition contained in the national law of the contracting authority or the economic operator. The EU definition of corruption includes the deliberate action of promising or giving, directly or through an intermediary, an advantage of any kind to an official or third party for him to act or refrain from acting in accordance with his duties or in the exercise of his official functions. It is broad enough to be consistent with the accepted generic definition of corruption, namely the abuse of public office for personal gain.

Reference to the definitions contained in the national laws is clearly desirable given the potential for different interpretations. Corruption is a notoriously difficult term to define and it is rare for national legislations, at least in Europe, to use it as a criminal act in itself. In most cases, national laws will prohibit corrupt actions through a series of more specific and precise offences, the breach of which will lead to conviction. These are usually based on the notion of a payment/receipt of a bribe in return for an advantage in the form of a benefit from the improper performance of, among other things, an official function.

Reference to national laws is also necessary given the requirements referred to above for the new rules to be implemented in the laws of the member states. Since this is not an EU debarment system per se but a set of conditions that will apply to any national debarment system within the EU, the precise details of the debarment system itself and the definitions used within that system will largely depend on how the provisions are implemented within national laws. In some countries, such as in Germany, that is already known but, in others, the debarment systems are still to be developed. Since the debarment and rehabilitation provisions of the new rules apply to both mandatory and discretionary exclusions, member states are bound to put measures in place, at least in respect of the mandatory exclusions.

For tenderers, this means that they will need to be familiar with the debarment *(and rehabilitation)* rules that apply in each of those member states in which operate or intend to operate. The EU rules indicate only the minimum conditions but do not set out at all the procedures that are to be followed or even, other than in general terms, the activities which will constitute corrupt activities in each or all of those member states. Whilst the original rules foresaw permanent exclusion, the new rules envisage that a maximum period of exclusion will be fixed by way of final judgment and, where that is not done, provides that the maximum period of exclusion should not exceed 5 years.

It is important to point out that the obligation to exclude a tenderer will also apply where the person convicted by final judgment is a member of the administrative, management or supervisory body of that economic operator or has powers of representation, decision or control therein. Whilst the actions of staff are likely to lead to debarment under systems compatible with the new rules, this provision also opens up the possibility that senior management employed by the tenderer who have been convicted of corruption, whether or not connected to the activities of their current employer *(the tenderer),* could put the tenderer into a debarment situation. As indicated above, it matters not any more when the events took place; the subsequent discovery of previous convictions could lead to the application of the mandatory exclusion rules at a later stage.

Finally, it is also open to member states to provide for a derogation from the mandatory exclusion, on an exceptional basis, for overriding reasons relating to the public interest such as public health or protection of the environment. Based on an examination of the

history of this derogation, it is clear that this may be used only in exceptional circumstances. In the preamble to the new rules, the example is given of urgently needed vaccines or emergency equipment that can only be purchased from a tenderer excluded under one of the mandatory grounds for exclusion. However, interpreting the meaning of 'public interest' *(or 'general interest', as it is expressed in the preamble)* may prove a fertile ground for litigation given the serious consequences of applying mandatory exclusions.

Discretionary Exclusion

In addition to the mandatory criteria for exclusion based on a final judgment, the rules also contain a series of discretionary grounds for exclusion which may be applied under less strict conditions. The discretionary rules for exclusion have also been amended in the new rules and, in some cases, may now be applied more freely *(e.g. without a judicial decision).* The grounds have been expanded and now include more provisions relating to integrity. For current purposes, we will concentrate on those grounds that focus on these questions of integrity.

Under these provisions, a contracting authority is permitted to exclude tenderers where they fall within certain grounds for exclusion but the member states may also require contracting authorities to exclude tenderers on these grounds. Doing so would establish an effective national debarment system which requires clear and precise procedural mechanisms to be put in place. Again, it means that the national laws at issue will need to be investigated in order to fully appreciate the extent of the applicable disqualification or debarment rules, especially since these are discretionary only under the EU rules.

The grounds for discretionary exclusion are now:

- where a contracting authority is aware of any violation of obligations established by Union or applicable international legislation in the field of social and labour law or environmental law;

- where a tenderer is the subject of insolvency or winding-up proceedings etc.;

- where the contracting authority can demonstrate by appropriate means that the tenderer is guilty of a grave professional misconduct, which renders its integrity questionable;

  This ground for exclusion was previously contained in two provisions, one of which was subject to a conviction by way of final judgment *(offences of professional conduct)* and the other relating to grave professional misconduct *(effectively the provision which has now been retained)* which could be proven by any means which the contracting authorities could demonstrate. The fact that the contracting now needs to demonstrate the existence of such a ground by appropriate means does not seem to change the burden of proof significantly. However, the new provision appears to limit this offence to one which renders its integrity questionable. This could allow for other grounds of misconduct *(such as those which relate to competence rather than integrity)* to escape debarment. It is the lack of integrity which now becomes the focus.

- where the contracting authority has sufficiently plausible indications to conclude that the tenderer has entered into agreements with other economic operators aimed at distorting competition;

Arguably, distortions of competition brought about by way of collusive practices are not strictly speaking examples of corruption, at least where corruption is defined as an incentive offered to incite a breach of official duty. Anti-competitive agreements take place exclusively on the supply side of the procurement equation *(although such agreements could, of course, be facilitated by official knowledge or complicity).* Nevertheless, many regulators are concerned with the effects of collusive agreements, notably bid-rigging, and are inclined to bundle such practices together with corrupt practices. It is, for example, the practice of the World Bank and other Development Banks. The EU definition of corruption can also be interpreted as covering such 'private' form of corruption.

- where a conflict of interest cannot be effectively remedied by other less intrusive measures;

One of the innovations of the new rules is the introduction of specific provisions relating to conflicts of interest which have not hitherto been regulated, although there has been European jurisprudence which has set out the parameters of conflicts in the context of public procurement.

Under the latest iteration of the rules, the concept of conflicts of interest now covers any situation where staff members of the contracting authority or of a procurement service provider acting on behalf of the contracting authority who are involved in the conduct of the procurement procedure or may influence the outcome of that procedure have, directly or indirectly, a financial, economic or other personal interest which might be perceived to compromise their impartiality and independence in the context of the procurement procedure. Member States are required to ensure that contracting authorities take appropriate measures to effectively prevent, identify and remedy conflicts of interests arising in the conduct of procurement procedures so as to avoid any distortion of competition and ensure equal treatment of all economic operators.

The concept also covers the situation described under the next ground for exclusion.

- where a distortion of competition from the prior involvement of the tenderers in the preparation of the procurement procedure cannot be remedied by other, less intrusive measures;

In many systems, such as that of the World Bank, an automatic conflict of interest is established whenever a tenderer or connected person has been involved upstream, e.g. in the preparation of specifications for a tendered project. EU jurisprudence has traditionally shied away from such assumptions and has required an actual conflict to arise whereby a situation of inequality is established under which an unfair competitive advantage is given to one of the tenderers. To some extent, this approach is now codified under the new rules. As a result, where a tenderer or an undertaking related to a tenderer has advised the contracting authority or has otherwise been involved in the preparation of the procurement procedure, the contracting authority is required to take appropriate measures to ensure that competition is not distorted by the participation of that tenderer.

Those measures will include the communication to the other tenderers of relevant information exchanged in the context of or resulting from the involvement of the tenderer in the preparation of the procurement procedure and the fixing of adequate time limits for the receipt of tenders. The tenderer concerned may only be excluded from the procedure where there are no other means to ensure compliance with the duty to observe the principle of equal treatment. Moreover, prior to any such exclusion, tenderers must be given the opportunity to prove that their involvement in preparing the procurement procedure is not capable of distorting competition.

This discretionary ground for exclusion is the corollary of this new conflict of interest provision, allowing disqualification where there are no other means of preserving equality of treatment. It is unlikely to be used as a general ground of debarment since the existence of inequality or distortions of competition will necessarily be determined in the context of a specific contract award procedure.

- where the tenderer has shown significant or persistent deficiencies in the performance of a substantive requirement under a prior public contract, a prior contract with a contracting authority or a prior concession contract which led to early termination of that prior contract, damages or other comparable sanctions;

This is a new provision which introduces a ground for exclusion which mirrors those contained in some national debarment systems. Ordinarily, information provided by tenderers is contract specific and related to the requirements of a particular contract award procedure. Failure to provide evidence of the successful completion of comparable contracts in the past has always been a ground for disqualification on the basis of insufficient technical capacity but this provision goes much further. It allows contracting authorities to take into account not only failures satisfactorily to complete prior contracts the tenderer has entered into with the contracting authority but also failures in respect of any public contract. Such information could, in practice, only be collected through some form of contractor registration or debarment system and allows the contracting authorities, for the first time, to take into account a much broader assessment of a tenderer's competence. Only such systems would provide evidence of persistent deficiencies of performance.

This ground for exclusion may be difficult to apply in practice since it does not explicitly require any court judgment to substantiate the poor performance. Where damages are or other sanctions are imposed by a court, deficient performance might be assumed but applying the exclusion in other cases may be more problematic. Would it apply where contractual liquidated damages are engaged *(and what effect does that have on the contractor's willingness to accept liquidated damages)* or where the parties accept early termination by mutual agreement? In the absence of a judicial decision, who decides whether the failure to complete a contract is due to the deficient performance of the contractor and not to the dilatory behaviour of the contracting authority? If the decision is left to the contracting authority, then it will be open to abuse. Where, as in the case of a national debarment system, such a decision is left to a third party (judicial or otherwise) then there is less scope for abuse. As with many of the issues discussed above, much will depend on the jurisdiction at play.

- where the tenderer has been guilty of serious misrepresentation in supplying the information required for the verification of the absence of grounds for exclusion or the fulfilment of the selection criteria, has withheld such information or is not able to

submit the required supporting documents;

- where the tenderer has undertaken to unduly influence the decision-making process of the contracting authority, to obtain confidential information that may confer upon it undue advantages in the procurement procedure or to negligently provide misleading information that may have a material influence on decisions concerning exclusion, selection or award.

This is another new provision and appears to provide something of a catch-all provision to cover cases of corrupt behaviour which are not otherwise caught by the ground for mandatory exclusion, above. It is rather vaguely drafted and does not seem to require any strong proof or evidence of the actions undertaken. Much may, in any event, depend on the national implementing measures in respect of corrupt practices, notably in respect of the definition of corrupt activities, but the provision is otherwise particularly open ended and open to abuse. In line with current jurisprudence, it is arguable that such a provision could not be applied directly, i.e. without implementing measures, because it is not unconditional or sufficiently precise and cannot be implemented without the exercise of discretion on the part of a member state.

Rehabilitation

As indicated above, one of the most novel aspects of the revised rules is the introduction of the possibility of rehabilitation. Under this provision a tenderer who would otherwise be excluded under the mandatory or discretionary grounds for exclusion may provide evidence to the effect that measures it has taken are sufficient to demonstrate its reliability despite the existence of a relevant ground for exclusion. This includes the possibility for a tenderer to request that compliance measures taken with a view to possible admission to the procurement procedure be examined.

This is a curiously worded provision and, although it appears to set up a system of rehabilitation similar to that included in some well-established debarment system, it fails in a number of respects.

The provision is retrospective in the sense that it applies to measures taken in response to a conviction or finding of misconduct before the contract award procedure has been concluded. It does not provide for prospective remedial action which would foresee continuing efforts to improve conduct. The ‘defence’ applies to action taken and not to be taken. Whilst the preamble to the new rules suggests that the purpose of this provision is to allow for the possibility that tenderers may adopt compliance measures aimed at remedying the consequences of any criminal offences or misconduct and at effectively preventing further occurrences of the misbehaviour, that is not the effect of this provision. It does not address the prevention of further occurrences of misbehaviour but the correction of past occurrences of misbehaviour. It thus fails in meeting the more general debrament objective of providing an incentive for future improvement and merely rewards the correction of a discovered offence.

This approach is compounded by a further provision under which a tenderer which has been excluded by final judgment from participating in procurement award procedures will not be entitled to make use of this possibility of rehabilitation during the period of

exclusion resulting from that judgment in the Member States where the judgment is effective. In the case of a mandatory exclusion, therefore, if the conviction itself refers to debarment *(or if that is an automatic effect)* or if debarment can only be made effective through a subsequent judgment, then rehabilitation is not available. In this respect, the EU approach is to use debarment as a punishment and not as an incentive for improvement since mandatorily excluded tenderers are debarred for the stated period of time *(no more than 5 years, unless the member state provides otherwise)*, regardless of any remedial action they may choose to take. It is only when the debarment is imposed by the contracting authority itself or a third party which is not capable of making a judicial decision *(i.e. in cases of discretionary exclusion)* that rehabilitation is available. This deprives rehabilitation of any useful effect where mandatory exclusion is applied and significantly reduces its impact. That does leave scope for rehabilitation in the case of discretionary exclusion and, given the ease with which such exclusion can be made under the new rules, that scope is broad.

The types of evidence that a tenderer may provide include proof that it has paid or undertaken to pay compensation in respect of any damage caused by the criminal offence or misconduct, clarified the facts and circumstances in a comprehensive manner by actively collaborating with the investigating authorities and taken concrete technical, organisational and personnel measures that are appropriate to prevent further criminal offences or misconduct. The preamble to the new rules states further that these measures may consist in particular in personnel and organisation measures such as the severance of all links with persons or organisations involved in the misbehaviour, appropriate staff reorganisation measures, the implementation of reporting and control systems, the creation of an internal audit structure to monitor compliance and the adoption of internal liability and compensation rules. In line with debarment systems generally, the measures taken by the tenderers will be evaluated taking into account the gravity and particular circumstances of the criminal offence or misconduct.

Where the evidence offered is considered sufficient, the tenderer concerned will not be excluded from the procurement procedure. Where the measures are considered to be insufficient, the tenderer must be given a statement of the reasons for that decision. It is for the member states to determine the exact procedural and substantive conditions for the application of this possibility, notably the identity of the authority that makes the decision on the sufficiency of evidence for the purposes of rehabilitation. The member states are, in particular, free to decide whether they want to leave it to the individual contracting authorities to make the relevant assessments or entrust other authorities at a central or decentralised level with this task.

Tendering in the Utilities Sector

The rules in the utilities sector, i.e. applicable to contracts awarded by public or private entities operating in the utility sectors of water, energy, transport and post, have always been more flexible than in the purely public sector and this flexibility has traditionally applied to the selection criteria also. In particular, contracting entities *(as the purchasers are known in the utilities sector)* have always been free to choose their own selection criteria subject to the general conditions of objectivity and transparency. They have also, however, been given the opportunity to rely on the selection criteria asset out in the rules applicable to the public sector. This has always been seen as a practical measure

allowing incorporation by utilities of acceptable selection rules into their tendering procedures without the need to reinvent the wheel.

This general approach has been maintained under the revised rules, although the introduction of the reinforced exclusionary rules and rehabilitation into the public sector rules makes this is a little less straightforward.

Where the contracting entity is also a contracting authority *(i.e. a public sector body),* then the new rules require that the selection criteria otherwise freely chosen must include the mandatory exclusion grounds described above on the same terms and conditions. As in the case of the public sector, it is also open to the member states themselves to require the contracting authorities to apply the discretionary exclusion grounds described above on the same terms and conditions. For the purposes of public sector entities, therefore, the same conditions are likely to apply in terms of debarment systems set up on a national basis. Again, however, this will depend on the systems of the member state at issue.

On the other hand, where the contracting entity is not a public sector body, it has a free choice as to whether or not to apply these mandatory exclusion rules and, where it does, this will again be on the same terms and conditions. This is done for practical reasons rather than out of concern for maintaining flexibility. As is made clear in the preamble to the new rules, contracting entities, which are not public sector contracting authorities, might not have access to indisputable proof of the matters referred to and so it would be inappropriate to force them to apply mandatory exclusion. If they do not have access to the information available to public sector entities, then they cannot be expected to apply the provisions in the same way. Of course, in those member states which maintain *(or establish)* national debarment systems which provide transparent information to the public, such information might be or become generally available and so could be applied by operators in the utility sectors where they so choose. This is not yet an obligation and could not be without a consistent and transparent system throughout the EU.

It is perhaps important that, in all of the cases mentioned above, the new rules state that mandatory and/or discretionary exclusion will apply on the same terms and conditions as in the public sector rules. There is otherwise no mention of the possibility of rehabilitation which appears to suggest that excluded tenderers cannot benefit from these new provisions. The reference to the “same terms and conditions” must, therefore, be read as including the provisions on rehabilitation. Whilst it is regrettable that this is not made explicit in the rules themselves, the preamble to the revised rules does disclose the intention of the legislator to apply the rehabilitation provisions into the utilities sector as well. It states that where contracting entities are obliged or choose to apply the exclusion criteria, they should apply the public sector rules concerning the possibility that tenderers adopt compliance measures aimed at remedying the consequences of any criminal offences or misconduct and at effectively preventing further occurrences of the misbehaviour.

One additional provision is included in respect of utility contracts which does not appear in the case of public sector contracts. Where contracting entities have referred to the public sector exclusion criteria, they must assess all entities on whose capacity the tenderer intends to rely *(e.g. joint venture partners, consortium members, group companies)* against the grounds for exclusion. If one if those entities is excluded, the contracting entity must require that the tenderer substitute a mandatorily excluded entity and may require it to substitute an entity excluded on discretionary grounds. This will then

provide some scope for the tenderer to remedy its choice or partner during the course of the contract award procedure and allows it greater scope for rehabilitation even where, as we saw in the public sector, a tenderer otherwise excluded on mandatory grounds stands no chance of relying on the rehabilitation provisions to remedy the situation.

What this Means for Tenderers

The biggest disappointment with the revised rules is that while they promise so much in terms of establishing for the first time a general system of debarment *(exclusion and rehabilitation),* they deliver so little. The rules provide *(notwithstanding some serious internal inconsistencies)* for some minimum safeguards and provide glimpses of what might eventually become the foundation of an accepted EU-wide debarment system but they continue to leave it to the member states to put these minimum conditions into action. From a tenderer's perspective, the introduction of these provisions means that the new rules will now have to be taken into account because ignoring them will have a significant effect on their ability to tender and on their likelihood of success. Yet, having caused the additional problems, these rules fail to provide a satisfactory solution.

Tenderers will now be obliged more than ever to have regard to the national legislations of those member states in which they intend to operate. They will need to do so in order to understand how 'corruption' is defined and thus what actions are prohibited and might lead to exclusion. Given the lack of consistency imposed at an EU level, it is the member states' rules that will define the conditions for mandatory and discretionary exclusions and the procedures that apply to debarment.

Of particular concern also are the softened grounds for discretionary exclusion *(which might be made mandatory by member states)* and the lack of rigour in the means of proof required; the effect of the past actions of senior management on the current business opportunities of the tenderers now employing them; the meaning of 'public interest' as a mechanism for avoiding mandatory exclusion; and, in the case of those bidding for contacts to be let by utility operators, the make-up on consortia and the participation of group companies.

The explicit reference to rehabilitation provides not merely an incentive but a requirement for companies doing business with the European public and utilities sectors to put in place internal compliance programmes to ensure that grounds of exclusion are avoided or, where that is not achieved, overcome. However, the continuing patchwork of EU minimum conditions and national implementing measures in 28 member states mean that the likelihood of debarment, the grounds for that debarment, the availability of rehabilitation and the extent of that rehabilitation *(and whether or not it is prospective)* will all be dependent on what is the kaleidoscope of European national laws.

The well-known Chinese curse is fulfilled: tenderers do now live in interesting times.

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